Birds of an ethnic feather: The impact of CEO-board cultural similarity on firm value and board effectiveness

SHAZERINNA ZAINAL OSMAN SHAH

PhD in Business and Management
Accounting & Finance Section
Cardiff Business School
Cardiff University

A Thesis Submitted in Fulfilment of the Requirements for
The Degree of Doctor of Philosophy

March 2021

Abstract

The thesis contributes to our understanding of the impact of CEO-board cultural similarity on firm valuation and the effectiveness of the board of directors in the Malaysian setting, where there are three clearly defined and dominant ethnic groups and thus distinctive cultural values. While prior studies have long emphasised the effect of social ties on governance outcomes, we know little about the effect of cultural ties between CEO and directors. Drawing from homophily and social identity theory, we hypothesise that similarity in cultural values may serve as an important conduit through which social connections and relationships are developed. This thesis postulates that cultural similarity can be an indicator of the existence of similar values and beliefs between CEO and directors, which can potentially be either detrimental or beneficial. Accordingly, this thesis investigates whether this new type of manager-director ties, resulting from cultural similarity, affects firm valuation and board monitoring effectiveness.

Using a large sample of publicly listed Malaysian firms over 2009-2016, we find that similarity in ethnic identities between the CEO and board of directors is detrimental to firm value. We also find a positive relationship between our proposed measure of board independence and firm value. These results suggest that cultural ties are value-relevant and act as a medium of CEO-board relationship, which consequently may impair the effectiveness of board independence. The cultural similarity is also shown to be associated with fewer board meetings and to be more detrimental when it applies to independent directors compared to executive directors. Our evidence suggests that cultural similarity impairs the monitoring function of a board and thus reduces shareholder value.

We also provide the potential causes of the negative valuation impact of CEO-board cultural similarity. Our findings highlight that the cultural similarity could also lead to weak board monitoring effectiveness and internal control over financial reporting as measured by earnings management practice. We also provide evidence that cultural similarity is associated with managerial entrenchment as reflected in the reduced involuntary CEO turnover. Overall, our evidence suggests that CEO-board cultural similarity reduces firm value and dampens the board's independence and monitoring

effectiveness. This thesis makes significant contributions to the nascent literature on corporate governance and has important implications for various stakeholders including shareholders, policymakers, and regulators.

Acknowledgements

In the name of Allah, the Most Beneficent, the Most Merciful, whose love and guidance made the completion of this thesis possible. All praises and thanks to Him, who blesses me with strength, wisdom and countless blessings in life as well as throughout my PhD journey.

I would like to express my deepest appreciation to my main supervisor**,** Professor Khelifa Mazouz, for his continuous support, guidance and immense knowledge throughout my PhD journey. You set such high expectations for me and trained me well to ensure that I could be a better researcher. Many thanks for your invaluable support.

I am extremely grateful to Dr Qingwei Wang for his willingness to act as my second supervisor and for his enthusiastic effort, concern and insightful advice. Indeed, you have been a great mentor to me and I will never forget your precious support.

I would also like to extend my deepest gratitude to my third supervisor, Dr Woon Sau Leung, for his support, guidance and expertise throughout my research journey, especially when I had a problem with my statistical analyses. You lifted my confidence and provided invaluable guidance, from the topic's selection to the final research process, as well as listened to all my research problems. I am forever indebted to you.

I thank my viva examiners, Professor Sabur Mollah and Dr Izidin El Kalak for the valuable advice to improve this thesis. I am also thankful to my annual review convener, Dr Kevin Evans, for his valuable support and kindness. Many thanks to the Associate Dean for Doctoral Studies, Professor Luigi M. De Luca, for his generous advice and support. Thanks to Dr Yusuf Karbhari for being there at the start of my PhD journey and all the lecturers in the Accounting and Finance department, who have shared their knowledge and helpful advice with me. I would also like to thank PhD office staff Lydia Taylor and Sol Salah, for their assistance with PhD administration matters, Aberconway librarians Stephen Ratcliffe and Susan Smith, for their support with DataStream and Capital IQ, and the school's computing technician Wayne Findlay, for his IT support. I am also grateful for the comments and advice received from all seminars and conferences: the 1st Summer School "Corporate Governance

and European Integration" in Ljubljana, Slovenia, 2nd PhD Symposium at Cardiff Business School, the British Accounting and Finance Association Doctoral Masterclass 2019 at the University of Birmingham, and the British Accounting and Finance Association in Emerging Economies (AFEE) Special Interest Group 19th Workshop Programme at the University of Economics, Prague, Czech Republic. I extend my deepest gratitude to Cardiff Business School, which has facilitated me with precious opportunities for studying and growing.

On a personal note, I am deeply indebted to my husband, Atif Ismail Samsudin, for his unconditional love, patience, care, understanding and encouragement. Throughout the ups and downs of my life, you never left my side. You made me smile, wiped away my tears, watched me succeed, saw me fail. Thank you for being my rock and my constant support system. I would never have made it without you. I am truly blessed to be your wife.

My heartfelt thanks to both of my lovely parents, Zainal Osman Shah and Rohayah Sulaiman, for all the prayers, love and support. You both have been the pillars of support, guidance and love of my life since the day I was born. You always pushed me to achieve higher and higher. Without you both, I'd never have been the person I am today. Thanks for everything, *Mama* and *Abah*! I am also grateful to my parents-in-law, Dr Samsudin Taib and Wan Zakiah, for their kindness, support and prayers. Special thanks to my brothers, Shahril Nizam and Muhammad Shafiq; my sister, Shaffinaz; my uncle, Ahmad Zambri; my siblings-in-law, Amir, Nadia, Aisyah, Ali Asyiqin and Aqilah; and the rest of my extended families and friends in Malaysia for their encouragement and moral support. I would also like to thank my PhD colleagues, Violina, Aqilah, Sarah, Bahana, Shandana, Julie, Jihee, Adel, Ian, Dimitri, Junyi, Ruth, Arbab, Soma, Rui Ye and Song; and my friends in Cardiff, Syalwani, Saodah, Yasmin, Anis Nirhana, Afifah, Aunt Maria, Miss Nida, Suenana, Suzanna, Izzati, Noyu, Shafikka, Kak Ayu, Diyana, Monika, Jenifer and Krishna for their great friendship, motivation and support. This PhD would not be possible without my sponsor, Universiti Sains Islam Malaysia and Malaysian Ministry of Higher Education. Thank you for the financial support and opportunity so that I could pursue my dream. Finally, many thanks to my ex-colleagues at Universiti Teknologi Mara, Tapah, Perak and my ex-lecturer at Universiti Utara Malaysia, Professor Wan Nordin, for all their invaluable advice and support.

Preface

A working paper which is based on Chapter 3 is circulated under the title of "CEO-board cultural similarity and firm value" and was under-reviewed by the Journal of Corporate Finance in 2020. The paper is co-authored with Professor Khelifa Mazouz, Dr Woon Sau Leung and Dr Qingwei Wang.

A further developed working paper is based on Chapter 4; it is circulated under the title of "CEO-board cultural similarity and earnings management" and it has received an acceptance with revisions decision from Corporate Governance: An International Review in 2021. The paper is co-authored with Professor Khelifa Mazouz and Dr Qingwei Wang.

Table of Contents

List of Tables

Chapter 2

Chapter 3

Chapter 4

Chapter 5

List of Figures

Chapter 2

Chapter 3

Chapter 1

Introduction

1.1 Motivation and objective

Boards of directors perform a pivotal corporate governance function. As a primary and prominent internal control mechanism, they are responsible for advising and counselling as well as overseeing and monitoring managers on behalf of firm shareholders and also protecting shareholders' interest (Jensen and Meckling 1976; Fama and Jensen 1983; Westphal 1999). Nevertheless, the effectiveness of boards of directors as monitors of Chief Executive Officer (CEO) behaviour, actions and performance continues to attract considerable attention in corporate governance literature, particularly after the recent wave of high-profile corporate scandals, which emphasises the numerous shortcomings in the governance system.

Furthermore, ample evidence from extant research suggests that boards of directors are less likely to perform effectively and objectively in monitoring the executives (e.g., Westphal and Zajac 1995; Westphal 1999; Hwang and Kim 2009; Nguyen 2012). Previous studies of the behavioural perspective within the corporate governance context contend that social-psychological factors such as directors' psychological biases (e.g., Westphal and Zajac 1995; Lee et al. 2014; Zhang et al. 2020) as well as social relationships between CEOs and directors plausibly limit board monitoring and firm governance (e.g., Hwang and Kim 2009; Nguyen 2012; Fracassi and Tate 2012). According to this sociology perspective, as one of the key governance actors, directors, in general, are "socially situated and socially constituted agencies" who make decisions and perform their roles hinged upon the "multiple roles and identities" implanted in their social relationship, norms, and lives (Westphal and Zajac 2013, p. 624; Zhang et al. 2020), which, subsequently, can compromise their governance roles.

Hence, a burgeoning body of governance literature has examined the implications of manager-director ties, particularly for the social relationship between CEO and board

of directors, which potentially elicit a director's psychological and sociological biases in monitoring and evaluating executives and subsequently jeopardise their governance roles and effectiveness. Most studies in CEO-board social relationships emphasise the relationship that is constructed via board interlocks, professional, education, and employment background, which has been characterised as achieved ties (e.g., Hwang and Kim 2009; Krishnan et al. 2011; Fracassi and Tate 2012). However, little attention has been given to the effects of such relationships that are elicited from ascribed status such as ethnicity or cultural ties, which are deeply rooted and inherited in individuals. As an important feature in reflecting an individual's life, cultural values play a key role in influencing their ways of living, thinking, socialising with others, and decision-making. Recent studies of corporate and behavioural finance show that individuals and nations with similar cultural values exhibit similar preferences and practices, and thus facilitate interaction and enhance connections. For instance, Guiso et al. (2009) find that cultural similarity fosters mutual trust and enhances economic exchange between nations. Moreover, the culture of a society acts as the "glue that holds its member together through a common language, dressing, food, religion, beliefs, aspirations, and challenges" (Abdullah 1996, p.3), and thus is more relevant to be a basis of group identity and homophilic relations among individuals.

The role of culture in finance and corporate governance is indeed a topical issue and has recently been the focus of a large body of literature. It has been argued that informal institutions such as societal culture are as important as formal institutions (e.g., laws and constitution) and play a significant role in explaining economic agencies' behaviour (Guiso et al. 2015). Most of these recent studies either view culture as a national attribute that captures cross-country differences in corporate practice (e.g., Shao et al. 2013; Zheng et al. 2013; Boubakri et al. 2016) or analyse the relationship between the cultural differences and corporate outcomes (e.g., Ahern et al. 2015; Shi and Tang 2015; Karoyli 2016). However, limited attention has been given to the cultural differences within corporate boards, which may influence the firm's governance and the effectiveness of the board of directors. So far, Frijns et al. (2016) have examined the impact of cultural diversity within UK corporate boards on firm performance and discovered that board cultural diversity lowers Tobin's Q. While the study provides evidence of how cultural differences within boards of directors affect firm performance, much uncertainty still exists about the effects of cultural differences

or similarities between CEO and board of directors on governance outcomes. In particular, the cultural similarity can be a signal of the presence of similar values and beliefs between CEO and directors, which can potentially dampen the effectiveness of the board of directors. Therefore, investigating the effects of cultural similarity between the CEO and board members and understanding the potential threats to objectivity stimulated by these cultural attributes are important as the effectiveness of boards of directors is essential for firm governance.

To fill the mentioned research gaps, this thesis integrates two related sociology theories (i.e., homophily theory and social identity theory) with the existing corporate governance theories (i.e., agency, resource dependence, and behaviour theory) to examine the main objective, which is to investigate whether and how cultural similarity between a CEO and directors affects firm valuation and the effectiveness of the board of directors. Due to the shared and common cultural values and attributes, previous research has also revealed that culturally similar individuals are more likely to be associates than are individuals who are culturally different (Byrne 1971; Kandel 1978; Leszcensky and Pink 2015, 2019), which is in line with the argument of McPherson et al.'s (2001) homophily theory. In agreement with homophily theory that advocates 'similarity breeds connection' and 'birds of a feather flock together' (McPherson et al. 2001), this thesis postulates that similarity in the cultural background could also catalyse and facilitate relationships among individuals. Thus, this thesis extends this line of inquiry to the context of corporate boards and offers new insights into how similarity in cultural backgrounds between the CEO and directors affects board oversight role and firm value.

In particular, this thesis posits that cultural similarity may be conducive to a close and emphatic relationship between the CEO and directors, thereby hindering the latter's exercising of due diligence in their monitoring task, which subsequently affects the firm performance. Nevertheless, the shared values may provide mutual trust, superior communications, greater information flows, and efficient decision-making between these two parties and, subsequently, an increase in firm value. Therefore, to understand the effects of CEO-board cultural similarity on firm value, these competing hypotheses will be elaborated and analysed in more depth in **Chapter 3** of this thesis. Furthermore, this thesis also relies on the social identity theory (Tajfel and Turner 1986) by postulating that cultural similarity can form cultural ties that can be a vital

basis of self-identity and social identity among individuals. Moreover, this can give rise to in-group biases and favouritism, which refers to in-group members extending preference and favour to each other over the out-group members in terms of behaviours, attitudes, preference, or perception (Turner et al. 1979; Hewstone et al. 2002). Therefore, due to the in-group favouritism and biases elicited from cultural ties, directors can be biased in executing their governance roles particularly in monitoring and evaluating the CEO's self-serving activities, thereby increasing managerial opportunism and entrenchment. Thus, to analyse the effect of CEO-board cultural similarity on the effectiveness of the board and managerial entrenchment, **Chapter 4** will discuss the effect of the similarity on financial reporting quality, as measured by earnings management, while **Chapter 5** will explain the influence of the cultural similarity on managerial entrenchment, as measured by involuntary CEO turnover.

Based on the above discussion, this thesis has one **main objective**, which is to investigate whether and how cultural similarity between a CEO and directors affects firm valuation and the effectiveness of the board of directors. To achieve this objective, the thesis will focus on the following questions. ***First,*** does CEO-board cultural similarity influence firm value? ***Second,*** what are the potential causes of the negative/positive valuation impact of CEO-board cultural similarity? ***Third,*** does CEO-board cultural similarity influence board independence and the effectiveness of the monitoring function of the board of directors? The objective and questions form the basis of our three empirical chapters in this thesis.

Answers to the overarching objective and questions are achieved by using unique hand-collected data of CEO-board cultural similarity in 621 Malaysian listed firms from 2009 to 2016. Culture itself is "fuzzy and difficult to define and construct" (Triandis et al. 1986, p.258), thereby it is difficult to measure due to its subjectivity and ambiguity. Take Hofstede's (2001) cultural dimensions as an example. Despite being the earliest and most widely cited cultural measure, it has been repeatedly criticised and challenged, particularly due to its use of national borders to capture cultural differences, and does not address the fact that many countries have different subcultures (McSweeney 2002a, 2002b; Baskerville 2003; House et al. 2004).

Thus, this thesis uses ethnic identity to measure culture. In general, ethnicity is not only a fundamental part of an individual's self-identity but also is one of the most

eminent identity cues that can distinguish individuals (Cokley 2007; Higginbotham and Andersen 2012; Andersen 2012). Hence, individuals from different ethnic origins own different attitudes, values, and norms that reflect their cultural heritages (Betancourt and Lopez 1993). Similarly, Desmet et al. (2017) find that ethnic identity is an important determinant of cultural norms, values, and preferences. Apart from influencing people's cultural beliefs and values, ethnicity may also influence the way board members interact and socialise. Therefore, in capturing the presence of CEO-board cultural similarity within a firm's corporate boards, the CEO's and other board of directors' ethnic identity has been used as an indicator of their cultural values.

1.2 Institutional framework: The choice of Malaysia

Malaysia provides a unique and suitable empirical setting to test the central hypotheses for several reasons:

First, anecdotal evidence suggests that the effect of social connections is more discernible when the market is comparatively inefficient, and when the formal system such as regulatory systems and legal enforcement are weak and underdeveloped (Xin and Pearce 1996; Haggard 2000; Allen et al. 2005). Given the constraints of informal systems and institutionalisation, informal institutions such as cultural and social factors may influence economic exchanges as well as corporate governance (Guiso et al. 2009). Under such environments, corporations and commercial activities are governed and characterised by relationship-based principles, where economic agents depend heavily on social ties and/or connections as opposed to arm's length principles in the Anglo-Saxon countries. Malaysia is a country that fits such a characterisation (Gomez et al. 1999; Haniffa and Cooke 2002; Gul et al. 2016). Such characteristics are likely to exert great influence on the governance structure of Malaysian firms.

Second, Malaysia is a melting pot of different ethnicities and cultures. It has three dominant ethnic groups, Malay, Chinese, and Indian, which have clearly defined and distinct cultural values.[1] Despite living together harmoniously as one nation, these ethnic groups: (i) have distinct cultural and religious heritages; and (ii) continue to

[1] Presently, the Malays are the largest ethnic group, making up half of the country's population, followed by the Chinese, with 23% of the population, whereas 7% are Indians and 1% are 'Others' (Department of Statistics Malaysia 2016).

maintain their separate identities and preserve their own cultures that influence their languages, customs, and behavioural patterns[2] (Sendut 1991; Abdullah 1992, McLaren and Rashid 2002; Rashid and Ho 2003). Furthermore, the majority of corporate boards in Malaysia consist of members from more than one ethnic group (Gul et al. 2016; Mohamad-Yusof 2018), hence ensuring the validity and the presence of CEO-board cultural ties. Thus, as a multicultural society that consists of clearly identifiable cultural values between the three main ethnic groups, which generally maintain their cultural values, Malaysia provides an interesting and relevant setting to examine the value relevance of the cultural similarity between directors and executives.

Third, the Malaysian setting is unique in the manner in which ethnic considerations have emerged to influence economic exchanges, social and political systems, and arm's length market forces, as well as government policy. For example, the Malaysian government introduced the New Economic Policy (NEP) to uphold the position and special treatment of the Malays as well as to rectify economic imbalances between the main ethnic groups by allowing them to increase their equity ownership up to 30%. By doing this, the government expects the corporate board's representation to reflect the ethnic composition of the nation (Mohamad-Yusof 2018). As a multicultural country, where cultural differences are unique to each ethnic group, as well as the launch of the affirmative policy, the Malaysian setting may be a significant influence on the composition of boards of directors and the social relationship of key governance actors within corporate boards. As culture elicited from customs and traditions that are "instilled in its people and might help explain why things are as they are" (Haniffa and Cooke 2002, p. 318), the societal values of multiethnic backgrounds in Malaysia may affect the relationship between the CEO and directors in different ways. Thus, an investigation in a unique setting like Malaysia will contribute to knowledge.

Finally, prior research shows that national culture influences corporate behaviour and decision-making (Guiso et al. 2006; Shao et al. 2010; Siegel et al. 2011; Zheng et al. 2012; Ahern et al. 2015; Boubakri and Saffar 2016). Since Malaysia is a multiracial country, no single national culture can reflect the cultural discrepancies of its very distinct ethnic groups. Thus, Malaysia represents an interesting context to examine

[2] Although other countries, such as the US, are also made up of highly cosmopolitan populations, it is less clear as to how ethnical and cultural differences between people can be measured among these countries.

how different cultural values of board members within corporate boards affect manager-director ties and how such ties affect organisational outcomes at the firm level.

1.3 Overview of thesis and contributions

This thesis is structured into six chapters. The following provides a brief overview of these chapters:

This **first chapter** introduces the motivation and objective of this thesis and provides justifications of the choice of Malaysia as the research setting. It also presents the overview of the thesis and contributions.

In the **second chapter**, the thesis outlines the vast literature on: (1) the role and theories about the board of directors, (2) the ramifications of CEO-director ties, (3) theories of cultural similarity, (4) the importance of culture in finance and corporate governance, and (5) the institutional background.

The **third chapter** addresses the first question and third question of the thesis. Specifically, it examines the effects of the cultural similarity between CEO and board of directors on firm value based on two competing hypotheses. While the cultural similarity between the CEO and board of directors may provide mutual trust, superior communications, greater information flows, and efficient decision-making, leading to increases in firm value, it can also be conducive to a close and emphatic relationship between them, thereby hindering the directors' exercising of due diligence in their monitoring task, which subsequently affects firm value.

Using ordinary least squares (OLS) regression, this chapter conducts a baseline analysis on the association between CEO-board cultural similarity and firm value, as measured by Tobin's Q. This chapter also conducts robustness checks by employing alternative model specifications and variable definitions. Furthermore, several endogeneity tests are also conducted by using firm fixed effect, propensity score matching model, and instrumental variables approach.

The chapter further delves into the additional analyses of whether greater CEO-board cultural similarity results in fewer board meetings by using the firm fixed effect model.

Motivated by existing studies that incorporate the social ties into the definition of true independence (e.g., Hwang and Kim 2009), this chapter then investigates the differential association between board independence and firm value when the formal measure of board independence (which does not consider CEO-board cultural ties) is replaced with the new measure of board independence. Under the new measure, a director is identified as independent if he or she is an independent director and also culturally independent from the CEO. Next, the chapter further explores whether the negative relation between cultural similarity and firm value differs among dependent (executive) and independent directors. Finally, the chapter further investigates whether the main results remain the same after controlling for political connections, as proxied by Malay CEOs and boards.

The **fourth chapter** addresses the second question of the thesis by identifying one of the potential causes of the negative valuation impact of CEO-board cultural similarity. Specifically, the chapter aims to explore whether the cultural similarity between the CEO and board of directors affects the quality of financial reporting. This chapter postulates that the presence of cultural similarity between the board and CEOs may jeopardise the board's monitoring role in ensuring fair and unbiased reporting. As a result of the board's reduced monitoring, the CEO is more likely to act and make decisions in their own interests; for example, engage in earnings management practice to smooth earnings.

Using OLS regression, this chapter conducts a baseline analysis on the association between CEO-board cultural similarity and earnings management, as measured by accrual-based earnings management. Several robustness checks and endogeneity concerns are also addressed.

This chapter further examines whether the positive effect remains consistent after controlling for CEO power. Arguing that the formally defined board independence does not account for the presence of cultural ties between CEOs and independent directors, this chapter further proposes a culturally-adjusted measure of board independence to investigate the extent to which the cultural independence between CEO and independent directors is relevant to earnings management practice. Next, this chapter considers whether the positive effect of cultural similarity on earnings management differs among the dependent (executive) and independent directors.

Finally, this thesis delves into further investigation of the implications of CEO-audit committee cultural similarity on earnings management.

In the **fifth chapter**, this thesis investigates another potential reason for the negative valuation impact of CEO-board cultural similarity by exploring whether the cultural similarity is associated with managerial entrenchment, as measured by involuntary CEO turnover. According to prior studies (Hwang and Kim 2009; Nguyen 2012; Kramarz and Thesmar 2013; Balsam et al. 2017), socially dependent boards have lower CEO turnover risk than firms whose boards are socially independent, and these studies also assert that the CEO-director ties are associated with reduced involuntary CEO turnover.

By employing a large panel dataset of the Malaysian listed firms between 2009 and 2016, this chapter conducts a logit regression analysis to analyse the association of CEO-board cultural similarity and involuntary turnover. This chapter also employs various alternative measurements and specifications as well as a robust to endogeneity test, which is conducted by using the instrumental variable approach.

This chapter is further interested in examining whether CEO-board cultural similarity is associated with lower turnover performance sensitivity. As the cultural ties with directors may facilitate bond, empathy, and trust between them, these CEOs are thus less likely to be replaced, even when they exhibit a poor performance. Next, we explore whether CEO duality affects the associations between cultural similarity and involuntary turnover. This chapter further analyses whether the effect of cultural similarity is equal when similarity is measured among the independent or executive directors.

The **sixth chapter** concludes this thesis. In this chapter, we summarise the key findings of the three empirical chapters, discuss the theoretical contributions and practical and policy implications, acknowledge the work's limitations, and provide areas for potential future research.

Overall, this thesis contributes to the nascent literature on corporate governance in several significant ways. First, it complements and extends corporate governance literature by introducing a new type of manager-director ties, arising from cultural similarity, and investigating how such ties affect firm valuation and the monitoring effectiveness of the board. In addition, it proposes a new measure of board

independence, which it is not in current regulations, by considering the presence of cultural ties and shows evidence that such ties affect the effectiveness of board independence. Second, it also considers cultural factors, which are often overlooked in the numerous literatures on the determinants of weak internal control and inefficient board monitoring. Third, this research complements and extends the limited studies on the role of culture within corporate governance by revealing that cultural ties between CEO and directors reduce the effectiveness of board monitoring and internal control, leading to decreases in firm value. Fourth, it also contributes to the extant literature on executives' incentives to manage earnings as well as CEO turnover by identifying a new mechanism through which CEOs can influence involuntary turnover and earnings management.

Chapter 2

Literature Review

This chapter will review the relevant broad works of literature and empirical studies on this topic to develop the theoretical background for this thesis. We will draw from sources in sociology, corporate governance, finance, and culture, among others, due to the interdisciplinary nature of this thesis. In this part, we first review the role and theories of the boards of directors. We will review two influential and traditional corporate governance theories, agency and resource dependence, as well as the new theory on boards of directors, behavioural theory, which are all related to our study. We then outline the impact of CEO-director ties by reviewing the existing literature on CEO-director ties. Next, we will also discuss the existing theories of cultural similarity, homophily, and social identity theories, together with the related existing empirical studies that are based on these theories. The implications of cultural ties will also be discussed in this chapter. We then review the role of culture in finance and corporate governance as well as highlight the weakness of the existing cultural dataset and measurement used in prior studies. The measurement of CEO-board cultural similarity in this thesis will also be discussed in this chapter. We also provide an institutional background of our study as well as the related Malaysian studies.

The chapter is structured as follows. **Section 2.1** provides an overview of the relevant theoretical foundations of the boards of directors. The impact of CEO-director ties is discussed in **Section 2.2**, followed by the existing theories of cultural similarity, homophily, and social identity theories, as well as the implications of cultural ties in Section **2.3**. **Section 2.4** reviews the role of culture in finance and corporate governance, discusses the weakness of the existing cultural dataset and measurement used in prior studies as well as the measurement of CEO-board cultural similarity used in this thesis. **Section 2.5** provides an institutional background and relevant Malaysian studies on this topic. Finally, **Section 2.6** highlights the summary of the chapter.

2.1 The roles and theories of the board of directors

The board of directors serves as a key internal governance mechanism. In general, it performs two principal functions: (i) advising and (ii) monitoring top management on behalf of the firm's shareholders and wider stakeholders (Jensen 1993; Westphal 1999; Adams and Ferreira 2007; Faleye et al. 2011). The advisory role includes assisting management in strategy formulation and implementation, as well as providing wise counsel in the other parts of vital decision-making (Pfeffer and Salancik 1978; Westphal 1999), while the monitoring role entails overseeing management to curtail managerial agency conflicts that result from the separation of ownership and control (Fama and Jensen 1983; Westphal 1999). Much of the empirical literature examining the effectiveness of the board of directors in performing these responsibilities is rooted primarily in two influential corporate governance theories of the board: (i) agency theory and (ii) resource dependence theory. Nevertheless, the last decade has witnessed a blossoming of governance research on the board that has relied on behavioural theory. Hence, in this section, the related central theoretical perspectives used to examine the roles of the board as well as the CEO-board relationship and social connections will be reviewed. Our main focus comprises three perspectives: agency, resource dependence, and behavioural theory.

2.1.1 Agency theory

Agency theory has been a dominant theoretical framework of corporate governance since the last decades of the 20th century. The publication of influential work on agency theory was pioneered by Alchian and Demsetz (1972), Ross (1973), Jensen and Meckling (1976), and Fama and Jensen (1983), explaining the firm as a 'nexus of contracts' between different parties such as suppliers, shareholders, directors, and customers. In the context of corporate governance, agency theory focuses on the separation of ownership and control between managers and shareholders. The agency view suggests that the principals (shareholders) contract with agents (managers), who are then expected to work and act accordingly on their behalf (Jensen and Meckling 1976). Nevertheless, a fundamental problem arises when there is a divergence or divorce of interests between these two parties, in which the managers may act in their self-interest at the expense of shareholders (Jensen and Meckling 1976; Eisenhardt 1989).

Therefore, as a vital internal control mechanism, boards play an important role in resolving this 'agency problem' by controlling potentially misaligned managers/CEOs through monitoring and incentives (Fama and Jensen 1983). According to prior studies, a board's competent monitoring is frequently accomplished by its structural, composition, and demographic characteristics such as the percentages of outside/independent directors (Westphal 1998; Dalton et al. 1998), whereas incentives are frequently determined through compensation such as incentive pay, stock options, and equity ownership (Schulze et al. 2001; Dalton et al. 2007). However, it is argued that such incentives can occasionally exacerbate the agency problems (Dalton et al. 2003; Bergstresser and Philippon 2006) and increase managers' self-serving behaviour (Denis et al. 2006). In outline, it is contended that monitoring, ownership, and incentives are amongst the important sources that can either mitigate or intensify agency cost, which could also affect the firm's strategy making, performance, and value.

Influenced by agency theory, prior studies on the CEO-board relationship have focused predominantly on the board's control and oversight over CEOs particularly in hindering managerial opportunism and in ensuring that CEOs execute their duties in accordance to the best interests of shareholders (Fama and Jensen 1983; Westphal 1999). Although qualitative research as well as review studies suggest that boards also provide advice and counsel to CEOs (Pfeffer and Salancik 1978; Lorsch and MacIver 1989; Boyd et al. 2011), their oversight and control roles are widely considered to be the most significant board function (Johnson et al. 1996). However, their oversight role can be hampered since not all directors on a board themselves are flawless agents to the shareholders. Likewise, they may also exacerbate the agency problems they were assigned to address. One of the pertinent factors that could induce this matter is the presence of both 'formal' and 'informal' relationship between CEO and board. As a matter of fact, prior studies document that the relationship between CEOs and boards permits the CEOs to exert influence over the boards, promoting a greater risk of managerial entrenchment and opportunism, thereby engendering agency costs and resulting in erosion of firm value (Daily and Dalton 1994; Westphal 1999).

Correspondingly, prior research has highlighted that a board's independence from the CEO is important in ensuring its monitoring and controlling effectiveness as it encourages the board to objectively monitor and discipline the CEO (Fama and Jensen

1983; Westphal 1999). In order to achieve such independence, firms usually rely crucially upon outside/independent directors, who are assumed to be less likely than insiders to conspire with managers to expropriate residual claimants (Fama and Jensen 1983; Westphal 1999). However, although outside board members are formally independent of top management as per regulations, numerous studies suggest that prevailing social, demographic, and psychological influences can jeopardise their willingness and ability to objectively and effectively monitor managerial performance (Westphal and Zajac 1995; Hwang and Kim 2009; Fracassi and Tate 2012; Lee et al. 2014). In sum, based on the agency theory lens, the oversight and monitoring role of boards over CEOs can be hindered via CEO-board relationship, which could worsen the agency cost as well as managerial, board, and corporate performance.

Even though agency theory has been widely used in many agency hypotheses with regard to CEO-board relationship, a numerous of studies have reported the conflicting results about the basic tenets of agency theory (Dalton et al. 1998; Tosi et al. 2000; Pepper and Gore 2012). For example, Tosi et al. (2000), in their meta-analysis of 137 empirical studies, revealed that incentive alignment as an explanatory agency concept for CEO compensation was at best inadequately supported by the results. In a more recent study, Frydman and Jenter (2010) contended that neither optimal contracting (agency theory) nor the managerial power hypothesis is fully consistent with the available results on the review studies of US executive compensation data. In a similar line, Kolb (2010) observed that agency theory performed poorly during the financial crisis while Aguilera et al. (2008) argued for its limited applicability to differential institutional settings since it has been widely applied and developed on the Anglo-American context, particularly in the US setting (Boyd et al. 2011). As Eisenhardt (1989, p.57) rightly points out, "agency theory is an important, yet controversial theory".

Such concerns and criticisms regarding agency theory have led to the emerging and growing developments of the new versions of agency theory, which have been considered to provide a better explanation of the connection among incentives, agent performance, firm performance, and the interests of shareholders. Such new branches of agency theory include social agency theory (Wiseman et al. 2012) and the behavioural agency theory (Wiseman and Gomez-Meija 1998; Pepper and Gore 2015). Therefore, although the original agency theory has contributed to

organisational thinking especially with regard to the treatment of information and its risk implications (Eisenhardt 1989), it is important to researchers in the area of CEO-board relationship to consider its limitations and other competing as well as supporting/extending theories which could also enhance research developments and contributions.

2.1.2 Resource dependence theory

Although agency theory is the prominent theory used in most of the empirical research on corporate governance (Zahra and Pearce 1989; Johnson et al. 1996; Dalton et al. 2007), resource dependence theory (RDT) has also become one of the most influential and appealing theories in understanding this area of research (Hillman et al. 2009). In their landmark publication of the *External Control of Organisations: A Resource Dependence Perspective*, leading RDT theorists Pfeffer and Salancik (1978) conceptualised that all firms critically depend on other firms and the external environment for the provision of important resources, in which such dependence is frequently reciprocal. Correspondingly, they suggest that such inter-organisational interdependencies can be achieved via board interlocks, joint ventures, alliances, and mergers and acquisitions (Pfeffer and Salancik 1978).

In the context of boards of directors, RDT is premised on the notion that board members are vital providers of resources such as expert advice, counsel, financing, and networks (Boyd 1990; Hillman et al. 2009). According to Pfeffer and Salancik (1978), boards of directors contribute four types of benefits to firms: (i) information via advice and counsel, (ii) channels to transfer information between the firm and external environment, (iii) privileged admission to resources, and (iv) legitimacy. In sum, apart from its role in monitoring and overseeing the managers, the board has been well-acknowledged to contribute to the firm by assisting the flow of information, which has been considered amongst the most valuable resources. Such contributions can be channelled through the other important functions that board provide, which are in advising and counselling the managers on strategic issues and decision-making (Westphal 1999).

RDT has been applied to understand CEO-board relationship especially in the case of the board's involvement and collaboration with the CEO via advising and counselling (Westphal 1999; Hillman et al. 2009; Boyd et al. 2011). In fact, numerous scholars

have employed the theory broadly either as a competing theory or a complementing theory against the prolific agency theory for their research hypotheses, particularly for understanding its effects on board/managerial performance, firm performance, and decision-making. For example, Westphal (1999) classifies two hypotheses of board involvement: the independent board, which is based on agency theory, and the collaborative model, which is based on RDT. In his seminal work on CEO-board relationship, he documents how social ties between the two parties are expected to differently affect the board's involvement in monitoring and advising interactions. His article, indeed, challenges the dominant agency perspective that CEO-board social ties decrease the involvement and effectiveness of independent directors and promote passive boards. Similarly, Boyd's (1995) study on the relationship between duality and performance was established from both RDT and agency theory. A more recent work, Fan et al. (2019)'s study of the implications of CEO-board friendship ties on firm performance, is also based in both RDT and agency theory. Their results reinforce the view that, while such relationship may induce effective counsel, it also can undermine the monitoring effectiveness of boards, leading to negative consequences for firm performance. Meanwhile, Ruigrok et al. (2006) used multifaceted theories in their study of the relationship between board characteristics and involvement in strategic decision-making. Such theories include the RDT itself, agency theory, institutional theory, and network theory.

Even though RDT has been widely employed in research on CEO-board relationship, most of the empirical research has neither explicitly demonstrated the advisory relations nor investigated how the relationship between these two parties may enhance a board's ability to execute this function properly (Westphal 1999; Boyd et al. 2011). In a more recent meta-analysis study on RDT, Drees and Heugens (2013) argue that the research based on the RDT has not always produced consistent results. In fact, evidence for this can be found in prior studies, as mentioned previously. As Casciaro and Pikorski (2005, p.167) observe, RDT is more of "an appealing metaphor than a foundation for testable empirical research". While scholars on CEO-board relationship are motivated to uncover the applicability of agency theory in different situations, types of relationships, and institutional settings, the different aspects of the resource provision effects are still open for empirical enquiry (Hillman et al. 2009; Boyd et al. 2011). As Hillman et al. (2009) suggested, a richer understanding of the specific

resources individual directors contribute to a board and their motivations to contribute them is also worth identifying. Furthermore, studies that utilise from multiple theories to investigate the simultaneous roles of the board and the multifaceted relationships between CEO and board could be an extension of analysis into the various resource dependence roles. However, such analyses could also be varying and erratic across countries and institutional settings. Hence, despite the strong support that exists for the application of RDT in the corporate governance research (Hillman et al. 2009), researchers must consider its limitations and advantages in explaining the effects of both a formal and an informal relationship between CEOs and boards.

2.1.3 Behavioural theory

Although many of the empirical studies on the board functions are based on these two different traditional theories (i.e., agency and RDT), as mentioned above, another flourishing body of governance research is rooted in behavioural and social network perspectives that focus on directors' psychological biases and social relationships rather than their economic rationality (Hillman et al. 2008; Westphal and Zajac 2013; Lee et al. 2014; Zhang et al. 2020). The theory of governance such as agency theory traditionally stems from an economic perspective that commonly assumes that economic rationality is the factor behind directors' behaviour and decisions, accentuating the influence of formal structures and systems in aligning the interests of shareholders and management (Westphal and Zajac 2013). Consequently, numerous studies in this tradition either implicitly or explicitly perceive the board's conduct as existing in a 'social vacuum' while, in fact, a board's effectiveness and environment depend strongly on "social-psychological processes, particularly [in relation] to group participation and interaction" (Forbes and Milliken 1999, p.492). As a result, these unaddressed elements of board may be the reason for the ambivalent results from the prior studies, especially in examining whether board independence improves monitoring and the provision of advice and counsel (Dalton et al. 1998; Boivie et al. 2016).

From behavioural and social network perspectives, directors' social-psychological and social connection factors play essential roles in influencing their behaviour and decision-making. In essence, such perspectives advocate that "the molecule of all social life is the socially constructed and socially situated individual, who lives, acts,

and develops within a set of proximate social relationships, institutions, norms, and rules" (Little 2012, p. 143). Based on this premise, Westphal and Zajac (2013) suggest that directors act as social actors in performing their oversight and advisory role. As 'socially situated' and 'socially constructed' agencies, their actions and motives could be driven by multiple roles and identities embedded in their social relationship and socialisation (Westphal and Zajac 2013; Zhang et al. 2020). Consequently, the social relationship and bond between these actors may affect the normative expectations and their actions are more likely to be governed by their communal norms, which develop mutual caring and trust, as opposed to exchange-based norms (Mills and Clark 1982; Hwang and Kim 2009; Lee et al. 2014). As a result, these social relationships and social psychological features have a potentially large impact on a director's monitory effectiveness, disciplinary capacity, level of involvement, advice-seeking, and information sharing (Westphal 1999; Adams and Ferreira 2007; Hwang and Kim 2009), which consequently may impair the firm value (Fracassi and Tate 2012; Lee et al. 2014; Goergen et al. 2015).

Consequently, a burgeoning literature has shed light on the impact of social identities and social-psychological factors on board decisions and the effectiveness of board monitoring. While many of these studies investigate the effects of social ties derived from the professional relationship such as mutual employment experience, educational level, and professional membership (e.g., Hwang and Kim 2009; Hoitash 2011; Fracassi and Tate 2012), some studies have also focused on how CEO-board informal ties such as political orientation, demographic similarities, and surname ties influence governance outcomes (e.g., Hoitash 2011; Goergen et al. 2015; Zhang et al. 2020). Nevertheless, the cultural ties between CEOs and directors have so far received little attention. As suggested by Kish-Gephart and Campbell (2015), the 'roots' of individuals, especially corporate decision-makers, have significant impacts on their decisions, preferences, and behaviours. Given that cultural background can substantially influence an individual's relationship with others (Pfeffer 1983; Hofstede 1984; North 1990; Cox et al. 1991) and that directors' and CEO's cultural background and values are regarded as part of their fundamental social identity, taking a behavioural and social network perspective on the CEO-board relationship calls for an investigation of how CEO-board cultural ties may influence governance outcomes and firm value. Compared with the professional and informal ties mentioned above, the

cultural ties or ethnic ties are more discernible to in- and out-group members and thus more likely to elicit individuals' psychological biases.

2.1.4 Power Circulation Theory

Power circulation theory was initially rooted in the classic political theories of elite circulation which has been developed by Mosca (1939), Michels| (1962) and Pareto (1963). The theory emphasises the political changing aspects among societal elites in which those elites are referred to the small group of powerful individuals who possess an unsymmetrical degree of treatment, influence, privilege, wealth, political power or skill in society (Pareto 1963). Prior studies have shown that the elites gain more power if they are highly integrated and collaborated. Nevertheless, the extent of integration differs depending on the degree of social homogeneity within a particular society. Although the organisations are governed by political elites or dominant coalitions, the positions of those elites do not remain.

For instance, in Malaysia, it was observable that elite groups are based on ethnicity attributes. While Malaysia has multi distinctive ethnic groups, the Malays and the Chinese were the most prevalent and elite ethnic groups in influencing and controlling the economic and political environment in Malaysia (Gomez 2002; Yatim et al. 2006). While the Malays dominate the country's politics and public services, the Chinese were mainly dominate the business and the economy in Malaysia (Sundaram 1989). As a majority of ethnic group in Malaysia, the Malays gain higher privileges, influences and treatments such as access to grants, loans, scholarships and civil servant positions. Meanwhile, ethnic Chinese, who only represent about 23.4% of the population, have maintained a huge presence in the corporate sector despite of the promulgation of New Economic Policy in 1970, which has been supportive to *Bumiputera* including the Malays. It was observable then that the Chinese capitalists gained economic prosperity but the Malays had restricted prospects to strive in the economic sphere, leading to resentment in the dominant ethnic group (Mariappan 2002; Yong 2004). Therefore, the unique combination of politics dominated by Malays and business dominated by Chinese making Malaysia unique research setting which varies from other Asian countries.

The power circulation theory has also been extended and applied to the corporate governance context. In the context of corporate boards, power circulation opposes the

premise that CEOs can maintain their power (Ocasio 1994; Shen and Cannella 2003; Combs et al. 2007). In particular, this theory suggests that the CEOs are managerial leaders that possibly susceptible of a dominant managerial coalition. Amongst the earliest and impactful studies of power circulation theory in corporate governance is that of Ocasio (1994). Ocasio (1994) examine the ability of CEOs to perpetuate their position over the firm's political coalition in the pressure of economic performance. Consistent with the theory, the study finds that poor performance emerges to motivate other managers to induce CEO succession. The study also shows that the likelihood of CEO dismissals among companies with poor performance increased with the proportion of executive directors. Based on power perspective, Shen and Canella (2002) shows that CEO origin, CEO tenure, non-CEO inside directors and top executive ownership reflects the authority of CEO, which could be significant contributor of CEO dismissals followed by inside succession. Meanwhile, Combs et al. (2007) examine how CEO power interacts with the power of other executives, particularly executives who are also board members. Drawing on agency and power circulation theories, they find that CEO power moderates the relationship between the composition of boards of directors and firm performance. Overall, these studies offer a contribution to understanding to the power circulation theory in the context of corporate boards.

Based on the power circulation theory, the CEOs may gain or reward power when they have the supports from the dominant managerial or directorial coalition. Therefore, based on the theory, we argue that CEOs gain more power when they have supports from managers or directors who have similar ethnic backgrounds. On the other hand, the CEOs may lose their power if the dominant managerial or directorial coalition are those who are not from the similar ethnic group. In the context of Malaysian board, the majority of board of directors consist of the ethnic Chinese even though the majority of population of Malaysia is dominated by the Malays. Thus, in the Malaysian corporate board, Chinese CEOs gain more advantage and power as the dominant managerial and directorial representatives are from ethnic Chinese.

2.2 The ramifications of CEO-director ties

The reasons, advantages, and effects of social ties between CEOs and their boards have been flourishingly studied in management, finance, and corporate governance research. Much of the research within this area has referred to CEO-board ties that have emerged and developed from various circumstances and forms, such as through the existence of mutual educational experiences, prior employment experiences, family or friendship relations, political orientations, or similar personality or social class, as well as demographic background (e.g., Westphal and Zajac 1995; Hwang and Kim 2009; Nguyen 2012; Lee et al. 2014; Goergen et al. 2015; Fan et al. 2019). These studies have mainly highlighted the influence of CEO-board social ties on governance outcomes such as board monitoring and effectiveness, and firm valuations, as well as strategic decision-making. Although prior studies shed valuable insights into the impacts of CEO-board ties, the findings are equivocal, in which such ties can have both bright and dark sides. **Table 2.1** provides a summary of the related literature on CEO-board director ties.

The major bright side of social ties is that they serve as great catalysts for better communication, mutual interpersonal trust, and personal understanding between individuals. In terms of corporate board context, prior studies show that social ties between CEO and directors enhance the board's key function in advising and providing counsel to the top management. Rooted in both Adams and Ferreira's (2007) theory of the friendly board and Westphal's (1999) collaborative board model, these studies contend with the notion that social ties facilitate an atmosphere conducive to a greater number of interaction and discussions concerning strategic issues as well as constitute an avenue for timelier and more valuable information sharing and governing between CEO and directors. More informed directors, in turn, provide better advice and counsel to the CEO, which results in quicker and more efficient decision-making. For example, Schmidt (2015) examines the informational effect of social ties between board executives. Using observable memberships of institutions outside the working environment between CEO and board members in constructing a proxy of social ties, he discovers that such ties are associated with the higher bidder in acquisition when the firm's advisory needs are high on acquisition strategies. Similarly, Cao et al. (2015) investigate the impact of the establishment of social ties on directors' informational advantage and find those directors who have social ties to the firm's

executives gain more firm-specific information than those without such connections. Hence, with the greater communication and valuable information flows between CEO and directors as results from the connections, the board is more likely to become more effective in exercising its advisory role.

Moreover, the information-sharing effects of CEO-board social ties also benefit the firm's important strategic decision-making such as innovation. As argued by Kang et al. (2018), the information exchanges gained between management and directors enhance the quality of the board's advisory role, thereby resulting in more successful innovation activities. Using CEO-director social connection as a proxy for board friendliness, they find that firms with friendly boards produce more patents and citations. The finding of the study reveals that a friendly board may add value through materially improving innovation outcomes. Similarly, Chahine and Goergen (2014) find that the social ties between top management and board of directors smooth social dealings that can increase the alignment of interests and preferences between them. They contend that IPO firms with such ties have mutual objective and consensus directions, and thereby are more likely to execute adequately articulated approaches to achieve better IPO performance. Using the data of all IPOs in the US market between 1997 and 2008, the study finds that top management-board ties increase pay-performance sensitivity, which in turn increases the IPO performance. Thus, consistent with the collaborative board model (Westphal 1999) and the theory of friendly boards (Adams and Ferreira 2007), these studies show the positive effect of CEO-board ties on decision-making and economic outcomes, which are more prevalent and value-added over a particular task, which is a result of the board's advisory role as opposed to its monitoring role (Hoitash 2011).

While the aforementioned studies have shown evidence of the beneficial effects of the social ties between CEO and board, such ties, however, can also have detrimental effects on governance and economic outcomes. Numerous studies suggest that CEO-director ties exhibit negative effects especially on the board's monitoring role, which is one of the important board functions as a key internal governance mechanism (e.g., Hwang and Kim 2009; Hoitash 2011; Nguyen 2012; Rose et al. 2014). These studies find that the presence of CEO-director social ties weakens the capacity of the board's monitoring mechanism, increases agency conflicts, and intensifies CEO opportunism and managerial entrenchment. The shared social bond between the two actors can

promote mutual caring, trust, openness, empathy, and acceptance that can develop dispassionate reciprocation, which affects the kind of oversight the board exerts over the CEO (Mills and Clark 1982; Westphal 1999). For instance, Hwang and Kim (2009) demonstrate that the existence of CEO-board social ties through mutual alma mater and military service inhibits board supervision and disciplinary actions, which can contribute to a greater managerial entrenchment such as lower CEO turnover and excess in compensation. Similar to Hwang and Kim (2009), Hoitash (2011) find evidence that excess CEO compensation is prevalent only in firms where social ties involve members of the compensation committee, implying that CEO-board social ties have the significant power to influence CEO compensation. In a similar vein, Nguyen (2012) reveals that a CEO is less likely to be terminated when s/he and several directors belong to the same social linkages, signifying that such ties significantly impact the effectiveness of boards of directors and increase managerial entrenchment, which is in line with Hwang and Kim (2009). Similarly, Rose et al. (2014) suggest that friendship ties between the CEO and board members can weaken the directors' independence and objectivity in monitoring and disciplining the CEO, and the public disclosure of such ties can worsen the effect.

While the above studies have shed light on the effect of CEO-director ties in board monitoring and managerial entrenchments, a few studies have also been carried out to examine the impact of such ties on financial reporting quality (Krishnan et al. 2011; Hwang and Kim 2012; Bruynseel and Cardinaels 2014) and corporate fraud (Khanna et al. 2015). Many of these studies have shown evidence that CEO-director ties weaken board independence and board monitoring, resulting in lower integrity of financial reporting quality, as reflected in an increase of earnings management. For instance, Krishnan et al. (2011) show that firms with more social ties between the CFO/CEO and the board are more prone to engage in earnings management in both the pre- and post-Sarbanes Oxley periods. While the function of ensuring the integrity of financial reporting quality is entrusted to the board, it is mainly the role of the audit committee within the board. By examining the effect of a CEO's social ties with audit committee members, Hwang and Kim (2012) also find evidence that these ties increase earnings management. Similarly, Bruynseels and Cardinaels (2014) also find evidence that social ties between CEO and audit committee reduce the quality of the audit committee's oversight, and that firms with such ties display a lower quality of financial

reporting, as reflected in the discipline of more earnings management and lower levels of audit effort. Although the aforementioned studies agreed that the CEO's social ties with the board as well as with the audit committee have detrimental effects on financial reporting quality, Hoitash (2011) show opposite results. They demonstrate that social ties between management and board members improve financial reporting quality and lower the likelihood of material weakness in internal control as well as the likelihood of financial restatements. Hoitash (2011) argue that such ties between them facilitate trust and openness and thus encourage a collaborative and information-sharing environment with management that results in enhanced internal control and financial reporting accuracy. Thus, whether detrimental or beneficial effects of CEO-director ties on financial reporting quality eventually dominate remains an open question.

Due to the reduced board effectiveness and monitoring as results of CEO-director ties, prior research has argued that such ties can also give a negative signal to the market, leading to negative implications for firm value (Fracassi and Tate 2012; Lee et al. 2014; Goergen et al. 2015; Fan et al. 2019). One of the earliest studies that examine the value implications of such ties is that of Fracassi and Tate (2012). Using a sample of large US firms, they find that the CEO-director' connections derived from mutual organisations, employment, and education experience destroy the firm value, especially if there are no other governance control mechanisms to substitute for board oversight and monitoring. The finding of the study is extended by Fan et al. (2019) in a more recent study, which reveals that social ties are linked to losses in firm value whereas professional ties are not. The study also demonstrates that both board roles (i.e., advising and monitoring) are plausible channels through which CEO-board friendship ties affect firm value and they are mainly complementary. Meanwhile, Khedmati et al. (2020) discover that social ties between independent directors weaken monitoring effectiveness, which in turn exacerbates the inefficient labour investment problems. While the above studies have focused on the value relevance of the CEO's social ties with board members that developed via mutual clubs, education, and employment experiences, relatively few studies have investigated the impact of demographic similarity between the CEO and board members on corporate governance outcomes. One of the earliest studies that does investigate the CEO-board demographic similarity is that of Westphal and Zajac (1995). The study developed a measure of demographic similarity between CEOs and directors such as age similarity

and found that greater similarity between the CEO and the board is related to a higher level of board composition and CEO compensation. Similarly, Goergen et al. (2015), in a more recent study, find comparable findings for German corporations. Focusing on the relations between the CEO and the chair, they indicate that age similarity lowers the firm value.

Prior studies have also shown that a similar background, view, personality, and belief between CEO and board members can lead to less effective corporate governance and have a detrimental effect on firm value. For instance, based on the broad evidence in the sociology literature that similarity breeds connections among people, which follows the homophily principle (McPherson et al. 2001), Lee et al. (2014) argue that similarity in political orientation could also act as a catalyst in growing ties among people. Using US corporate boards as a sample, Lee et al. (2014) show that the political alignment between CEO and independent directors reduces firm value and operating profitability by increasing agency conflicts and managerial entrenchment. Zhu and Chen (2015) also show the similarity in narcissistic tendency (narcissisms) between CEOs and their boards on new director selection and their strategic decisions. In a more recent study, Zhang et al. (2020) reveal that innate ties such as surname ties between CEO and board members lead to increased agency costs. Based on the behavioural perspectives, these studies successfully demonstrate that CEO and directors' social identities elicited via social-psychological factors can influence the effectiveness of board monitoring and board decisions. While prior research has investigated the impact of similarity in values, personality, and beliefs between these two corporate actors on corporate governance and organisational outcomes, no previous study has investigated the effect of the CEO-board ethnicity and cultural similarity on governance outcomes. Since ethnicity or culture is amongst the most important salient characteristics owned by individuals, this study fills the gap in the literature by investigating the role of CEO-board cultural similarity in the value-creation process and the effectiveness of board monitoring.

Table 2. 1: Empirical studies of the CEO-board relationship

Authors	Country	Research context	Independent variable	Dependent variables	Key findings
Westphal and Zajac (1995)	US	Director selection	CEO-board demographic similarity	CEO compensation contract	Greater demographic similarity between the CEO and the board is likely to result in more generous CEO compensation contracts.
Hwang and Kim (2009)	US	Board independence, social ties, executive compensation	Conventionally and socially independent board to CEO	CEO compensation, pay-performance sensitivity, turnover performance sensitivity	Firms whose boards are conventionally and socially independent award a significantly lower level of compensation, exhibit stronger pay-performance sensitivity, and exhibit stronger turnover-performance sensitivity than firms whose boards are only conventionally independent.
Krishnan et al. (2011)	US	CFO/CEO, corporate boards, social ties, earnings management, Sarbanes-Oxley	CFO/CEO-independent directors' social ties as measured from prior employment, education and other activities	Earnings management	There is a positive relation between CFO/CEO-board social ties and earnings management. Still, the increase in managerial/board risk aversion since SOX appears to have negated the effect of social ties on earnings management in the post-SOX period.
Hoitash (2011)	US	CEO compensation, corporate governance, financial reporting quality, independent directors, social network, social ties	Director-management social ties	CEO compensation, material weakness	Social ties are associated with higher managerial compensation; financial reporting quality is improved when social ties exist. The likelihood of material weaknesses in internal controls and the likelihood of financial restatements are lower in companies with social ties.
Nguyen (2012)	France	Social networks, CEO turnover, boards of directors, firm performance, corporate governance	CEO-director's shared social network	CEO turnover	When the CEO and a number of directors belong to the same social networks, the CEO is less likely to be dismissed for poor performance.
Hwang and Kim (2012)	US	Audit committee, social ties, earnings management	CEO-audit committee's social ties as measured by shared quality and experience	Earnings management as measured by discretionary accruals	There is a substantially stronger, positive relation between abnormal (i.e., discretionary) accruals and the extent of an audit committee's connection to the CEO when social ties are considered in addition to the conventional ties. An audit committee's social affiliation is associated with an increased discontinuity in the earnings distribution surrounding earnings targets.

Fracassi and Tate (2012)	US	External network, internal governance, firm value	CEO-director network	Firm value	CEO-director ties reduce firm value, particularly in the absence of other governance mechanisms to substitute board oversight.
Lee et al. (2014)	US	Political alignment between top management and directors, firm value, board independence, managerial entrenchment, corporate fraud	Alignment in political orientation between the CEO and independent directors	Firm value, operating profitability, CEO dismissal, CEO-pay performance sensitivity, accounting fraud	Alignment in political orientation between the CEO and independent directors is associated with lower firm valuations, lower operating profitability, and increased internal agency conflicts such as a reduced likelihood of dismissing poorly performing CEOs, a lower CEO pay-performance sensitivity, and a greater likelihood of accounting fraud.
Chahine and Goergen (2014)	US	Initial public offering, family ties, social ties, pay-performance sensitivity (PPS), homophily	Top management-board members' family and social ties	Pay-performance sensitivity	Both social ties and family ties increase PPS. In turn, PPS improves IPO performance. More importantly, greater PPS increases the positive effect of social ties on IPO performance whereas it reduces the negative effect of family ties.
Rose et al. (2014)	US	Corporate governance, earnings management, directors disclosure, friendship ties, research and development (R&D)	CEO-director's friendship ties	R&D	Board members who have friendship ties with the CEO are more willing to support reductions to research and development (R&D) expenses that increase net income to a level that triggers a bonus for the CEO.
Bruynseels and Cardinaels (2014)	US	Social ties, financial reporting quality, audit committee monitoring	CEO-audit committee social ties	Oversight quality	Social ties between CEOs and the audit committee may reduce the quality of the audit committee's oversight. This negative effect is particularly evident when CEOs and audit committee members share friendship ties.
Cao et al. (2015)	US	Social networks, insider trading, independent directors	Social connections between independent directors and firm's senior executives	Insider trading profitability	Independent directors socially connected to their firms' senior executives earn significantly higher returns than unconnected independent directors in stock sales transactions. The network effect on independent directors' trading profitability is stronger in firms with higher information asymmetry and with more powerful executives.

Khanna et al. (2015)	US	Network ties, corporate fraud	Appointment-based CEO connections	Fraud	Appointment-based CEO connectedness is positively related to the likelihood of corporate fraud and negatively related to the likelihood of detection given fraud.
Zhu and Chen (2015)	US	Director selection, CEO power, narcissism and personality, similar-attraction theory, triads and social structure	CEO's narcissistic tendency	New director's similarity to CEO in narcissism	CEOs favour new directors who are similar in narcissistic tendency or have prior experience with other similarly narcissistic CEOs.
Schmidt (2015)	US	Board independence, social ties, mergers and acquisition	CEO-board social ties as measured by shared membership and institutions outside working environment	Takeover returns	Social ties are associated with higher bidder announcement returns when the potential value of board advice is high, but with lower returns when monitoring needs are high.
Goergen et al. (2015)	Germany	Chair-CEO relation, cognitive conflict, monitoring, board meetings, firm Value	Chair-CEO age dissimilarity	Firm value as measured by Tobin's Q and the number of supervisory meetings to measure monitoring intensity	This study shows that greater age dissimilarity between the chair and the CEO, particularly in the form of a generational age gap, leads to more intensive monitoring and higher firm value.
Kang et al. (2018)	US	Corporate innovation, firm value	Board friendliness as measured by CEO-director social connections	Performance of innovation activity	Firms with friendly boards create more patents and citations. The positive relation between friendly boards and innovation is more pronounced when firms' advisory needs are higher or when firms operate in innovative industries. Friendly boards are also associated with higher firm value, especially when firms have higher advisory needs or when innovation is an important source of firm value.
Fan et al. (2019)	US	Board-CEO friendship ties, firm value, agency theory	CEO-director friendship ties as measured by shared educational background or memberships of social organisation	Firm value as measured by Tobin's Q and Total Q	Board-CEO friendship ties have a negative and economically meaningful impact on firm value, as measured by Tobin's Q and Total Q. Regarding potential channels of firm value, the study shows that the negative influence of board-CEO friendship ties on firm value is reduced in firms with greater board advising requirements but intensified in firms with higher board monitoring needs.

Khedmati et al. (2020)	US	Labour investment, monitoring, CEOs, directors	CEO-director ties (education, employment, and friendship ties)	Inefficient labour investment	CEOs who have strong ties with independent board members are associated with inefficient labour investment. The effect is stronger in firms that rely more on skilled labour and those that are financially constrained, in which inefficient labour investment exacerbates labour cost stickiness
Zhang et al. (2020)	China	Surname ties, agency costs, corporate governance, social identity theory, agency theory	CEO-board surname ties	Agency costs	CEO-board surname ties increase agency costs. This relationship weakens when firms have strong monitoring by shareholders and when directors' or supervisors' interests are closely aligned with firm value. This study indicates that directors tend to act as social group members when they share the same surname with the CEO. Such directors are more likely to act economically when they face monitoring from shareholders or supervisors or when their interests are aligned with firm value.

Source: Compiled by the researcher

2.3 Theories of cultural similarity

"We love those who are like ourselves"

-Aristotle

"Similarity begets friendship"

-Plato

2.3.1 Homophily theory

Many sociology and psychology scholars have long argued that people prefer to associate with similar others (Lazarsfeld and Merton 1954; McPherson et al. 2001). According to this similar/attraction theory or homophily principle, people prefer to interact and communicate with others who possess similar characteristics, backgrounds, values, and attitudes (Lazarsfeld and Merton 1954; Byrne 1997; McPherson et al. 2001; Montoya et al. 2008). In turn, the similarity in such features increases mutual understanding and liking, which also facilitates the formation of a close relationship. In fact, such close formation built from the homophily principle has been a ubiquitous presence in a variety of settings such as school, work, marriage, and friendship. The homophily theory has two dimensions: (i) status homophily, in which similarity is based on formal ascribed status, such as sex, age, ethnicity, religion, and education; and (ii) value homophily, which is based on values, attitudes, and beliefs, such as political orientation (McPherson et al. 2001). Both dimensions suggest that the salient attributes between people would moderate the vagueness of interpersonal interaction and assist people to interact and communicate with ease, confidence, and trust, prompting effective information sharing and collaborations.

Yet, despite the pervasive evidence that people are prone to bond with others who share similar characteristics, the value ramification of this inclination remains unclear. Broadly speaking, the more characteristics a pair of individuals share in common, the better the synergy between them. This synergistic performance may result from their ability to communicate and make consensual validations and decisions in an effective and timely manner (McPherson et al. 2001; Brechwald and Prinstein 2011). Furthermore, this type of social structure may contribute to the social capital, as it allows occupants to access more diverse and value-relevant information (Lin et al.

2001). Thus, the reasoning for the homophily theory is quite simple and clear-cut: 'similarity breeds connections' and 'birds of a feather flock together' (McPherson et al. 2001). However, homophily may be subject to several illuminating weaknesses, including the induction of social agreement and groupthink, which can hamper innovation and effective decision-making (Arrow et al. 2000). In addition, individuals with common characteristics may choose to set their targets and standards similar to others in the group to preserve their social capital. These negative attitudes may, in turn, undermine the group's performance and its ability to meet its objectives. Therefore, homophily is a double-edged sword: it brings people with similar characteristics closer together but pushes those with different characteristics away from each other.

In the context of cultural similarity, prior studies have shown that culturally similar individuals are more likely to be associates than are individuals who are culturally different (Byrne 1971; Kandel 1978; Leszczensky and Pink 2015, 2019). In addition, studies have constantly shown that ethnicity and race, which are the salient predictors for cultural values, are indeed among the most crucial sources of homophily in different kinds of associations for both children and adults (McPherson et al. 2001; Smith et al. 2014; Leszczensky and Pink 2015, 2019). In fact, Alba (1990) suggests that attitudes, behaviours, preferences, and values are frequently related to, or even rooted in, ethnicity, as demonstrated by rich sets of group-specific traditions, norms, customs, and opinions. In numerous cases, a shared ethnicity is also embedded via a common language and group history that is frequently built by mutual interests and experiences (Phinney 1990). For example, numerous studies have shown that, even in ethnically or culturally mixed schools, youths are more likely to associate with peers of the same ethnic group (Quillian and Campbell 2003; Smith et al. 2014; Leszczensky and Pink 2015, 2019). Hence, the theoretical concept of cultural or ethnic homophily relies on the argument that members of the same cultural or ethnic group have more in common than do members of different cultural or ethnic groups.

2.3.2 Empirical research on corporate governance using homophily theory

In this section, we review several empirical studies on corporate governance that have been well-influenced by homophily theory in framing various hypotheses to obtain results. These studies have been conducted in the context of many settings and almost

all utilise various forms of homophilic relationship such as education, employment, age, gender, geography, ethnicity, religion, and many more (e.g., Westphal and Zajac 1995; Hwang and Kim 2009; Lee et al. 2014; Goergen et al. 2015). Such a homophilic relationship between corporate governance actors has been mainly suggested to establish an informal, personal, and close tie between the actors which could affect their strategy, behaviours, decision-making, and performance. Since most of these studies form the basis of our study and highlight the influence of homophily perspectives on corporate decisions and governance, it is necessary to discuss their methodology and findings on various aspects of organisational governance separately and in detail.

One of the earliest studies that have utilised the concept of homophily within the corporate governance context is that of Westphal and Zajac (1995). In a comprehensive and longitudinal analysis of Fortune/Forbes 500 companies, they document that powerful corporate governance actors are more likely to enhance their coalition of support and collaboration by hiring people with similar demographic connections. These findings support the notion that demographic similarities between CEO and board members are associated with the strategy used to select directors and managerial entrenchment. This view is also supported by Hwang and Kim (2009), who provide evidence that CEOs select directors with similar observable characteristics (i.e., mutual alma mater, military service, academic discipline, regional origin, and industry) and these CEO-board personal connections, which have formed from the shared characteristics and experiences, have a significant impact on the board's monitory and disciplinary effectiveness. The findings also suggest that a board's independent-mindedness relies not only on the formal or conventional ties to the CEO but also on the social ties which have been established due to the homophilic relations between CEO and board. Again, using similar proxies to measure CEO-audit committee social ties as their previous studies on CEO-board social ties and board effectiveness, Hwang and Kim (2012) find that the informal connections between CEO and audit committee members also have a significant effect on the earnings management and creative accounting practices.

Although most of the previous studies on homophily theory have been developed based on US samples, there is also a well-established strand of literature on non-US settings. Since corporate governance research outcomes may vary due to large

differences in legal, institutional, and social background, it is also important to review significant studies from various countries and institutional settings to gain more understanding of the effects of the homophily perspective. One of the studies in a non-US setting was conducted by Goergen et al. (2015), who examine the implications of age dissimilarity between the chair of the board of directors and the CEO on firm performance and the need for monitoring. Using German corporate boards as a research setting due to the country's two-tier board system, they provide evidence that, the lesser the age similarity between the two parties, the better the performance of the firm, and the higher the number of board meetings. Meanwhile, Nguyen (2012) has examined the effect of social ties on the effectiveness of boards of directors by using a sample of the largest listed firms in France. He argues that common membership from an elite college education and civil service constitutes the measure of the close social relationship between a CEO and boards, which significantly undermines the effectiveness of the board of directors. In the context of Chinese corporations, Zhang et al. (2020) argue that ascribed or innate social ties (e.g., surname) are more likely to form a group identity. Drawing on social identity theory and agency theory, their findings show that CEO-board surname ties result in increased agency costs and lower firm value. Meanwhile, in a similar research setting, Kong et al. (2020) find that the hometown connection of CEO and suppliers can also form a basic source of social ties, which consequently benefits firms to access trade credits.

Numerous studies have also focused on the role of salient values and beliefs similarities between CEOs and their boards in corporate governance. This strand of research argues that such homophilic relations can increase communication and empathy between board members and the CEO. This may, in turn, result in quicker and more efficient decision-making and subsequently higher firm value (Lee et al. 2014). However, the shared beliefs and values between the CEO and other directors may also impair board independence and monitoring effectiveness. Using US corporate boards as a sample, Lee et al. (2014) show that the political alignment between CEO and independent directors reduces firm value and operating profitability by increasing agency conflicts and managerial entrenchment. Zhu and Chen (2015) also show the similarity in narcissistic tendency (narcissisms) between CEOs and their boards on new director selection and their strategic decisions. They argue that those who have similar narcissistic levels tend to work together and substantially influence

the relationship among them. The research finding shows that narcissistic tendency similarity between top management and directors influences the risk-taking spending, director selection, and board control over management. Collectively, these studies provide important insights on how demographic and social-psychological similarities between CEO and board of directors weaken firm and governance performance in various settings by using various measurements as the basis for the CEO-board social ties.

Although prior research has investigated the impact of homophily or similarity in overt characteristics and intangible characteristics including shared values, personality, and beliefs on firm and governance performance, there has been relatively little work concerning the effect of cultural similarity on organisational outcomes. One of the few works that have examined the effect of cultural similarity is that of Shi and Tang (2015). Using religious and ethnic similarity to proxy for cultural similarity across US states, they find national cultural similarity between partner firms has a positive impact on cross-border alliance formation and performance. This study, however, has mainly focused on cross-firm cultural connections in driving corporate decisions. Relatively little is known about the role of within-firm cultural ties, and no single study exists to investigate the impact of cultural ties/similarity between CEO and board of directors. Therefore, since culture is amongst the most important salient characteristics owned by individuals, this study seeks to fill the gap in the literature by investigating the role of CEO-board cultural similarity in the value-creation process.

2.3.3 Social identity theory (SIT)

Social identity theory (SIT) is an influential social psychology theory which focuses on intergroup relations, group processes, and the social self. Significant work on SIT originated with Henri Tajfel in the early 1970s in Britain, and was then advanced and entirely formulated in collaboration with John Turner and others in the mid- to late 1970s (Tajfel and Turner 1979). According to Tajfel (1972, p.292), social identity is defined as "the individual's knowledge that he belongs to certain social groups together with some emotional and value significance to him and of this group membership". Furthermore, the theory suggests that individuals tend to identify themselves and others into various kinds of social categories such as organisational membership, family, sports team, religious affiliations, gender, nationalities, ethnic

groups, and age cohort (Tajfel and Turner 1986). Generally, it describes the mechanisms that social identities influence people's attitudes and behaviours towards their in-group and the out-group. It is essential among group members "to differentiate their groups positively from others to achieve a positive social identity" (Turner et al. 1987, p.42). However, such self-categorisation and social identification could lead to the emergence of in-group favouritism, intergroup bias, and out-group discrimination (Tajfel 1982; Brewer 1999). As the maintenance of in-group identity is important to an individual's self-esteem, the need to attain positive group distinctiveness encourages individuals to compare their in-group with the out-group and to recognise the in-group as favourable (Brewer and Brown 1998; Brewer 1999). Therefore, the more strongly individuals identify with their group, the more biased and less favourable attitudes they demonstrate towards dissimilar groups.

In fact, evidence has been ubiquitous in explaining the SIT approach of in-group preference or favouritism. For instance, in a multiracial American setting (i.e., White, Black, and Asian), college students with high in-group bias were significantly more negative towards members of other or different ethnic groups concerning their attitudes, behaviours, and cognitive judgments relating to several social matters (Tzeng and Jackson 1994). Drawing from SIT, a substantial body of research also has focused on cultural, racial, and ethnic identity. The research mostly encompasses ethnic identity (Phinney 1990), racial identity (Sellers et al. 1998), and collective self-esteem (Luhtanen and Crocker 1992). The main idea of these theories is quite similar, which suggests that people like the 'we-group' better and think it is superior to 'other-groups'. However, to some extent, the theories are distinctive. According to Cokley (2007), ethnic identity signifies "how individuals see themselves relative to their cultural beliefs, values, and behaviours" (p.225) and racial identity signifies "how individuals construct their identities in response to an oppressive and highly racialised society (p.225). Nevertheless, both concepts incorporate learning and understanding about one's cultural group, embracing cultural behaviours and values, and feeling that one belongs to a specific group (Casey-Cannon et al. 2011). As a result, the more strongly people identify, embrace, and belong to their cultural group, the more discriminate and unfavourable behaviours and perceptions they hold towards the dissimilar cultural group.

Drawing from SIT and intergroup bias, prior research suggests that people with similar cultures are more likely to identify each other as in-group members (Hewstone et al. 2002; Shi and Tang 2015). Furthermore, such identification is influential and strong when people consider membership in a particular cultural group to be central to their self-concept and they feel strong emotional connections to the group. The in-group favouritism, which is a product of SIT, encourages people with similar cultures to display higher levels of mutual trust, in-group liking, cohesion, cooperation, altruism, and attraction (Tajfel et al. 1979; Deschamps and Brown 1983; Turner 1984; Turner et al. 1987). In addition, it also enables people to conceive of and feel loyal to their cultural group, which could lead to a pessimistic view of intergroup harmony (Tajfel 1982; Tajfel and Turner 1986), negative stereotypes (Horwitz and Rabbie 1982), social distance (Sunar 1978; Smith 1983), and bias (Turner 1984) towards people with a dissimilar cultural group (i.e., the out-group). Thus, such a notion based on SIT, especially in explaining the effect of cultural identity, may offer a fresh perspective on a number of critical organisational and management issues. As a matter of fact, SIT has been applied to explain various issues of interests such as organisational socialisation, role conflict, intergroup relations, intergroup conflict, conformity to group norms, and the factors that promote the categorisation and identification of oneself and others into groups (Ashforth and Mael 1989; Huddy 2001).

2.3.4 Empirical research on corporate governance using social identity theory

Several important studies have examined boards' behaviour, functions, and effectiveness by integrating and employing various overarching organisational theories from the influential agency theory to resource dependence theory in explaining the empirical findings. In this section, we aim to review the extant studies within the corporate governance and boards' context which have focused on and utilised social identity theory (Tajfel et al. 1979; Tajfel and Turner 1986), one of the most established and widely studied theories in the realm of social psychology. Due to the ubiquitous presence of multiple salient categories and groups within a firm as well as a board, it is argued that corporate governance actors such as managers and directors are also "socially situated and constituted agencies", who make decisions and judgments depending on their "multiple roles and identities" embedded in their social lives and relationships (Westphal and Zajac 2013, p.624; Zhang et al. 2020).

A flourishing body of governance research indicates that these corporate actors within firms usually classify each other into social groups which can be elicited from various social identities such as organisational (Hillman et al. 2008; Veltrop et al. 2018), family (Deephouse and Jaskiewicz 2013), gender (Terjesen and Sealy 2016), race, and surnames (Zhang et al. 2020). These highly salient social identities or categories can capitalise on perceptions of intra-category similarities and intra-category differences (Hogg and Terry 2000). A superordinate group where various categories exist, such as a board of directors, can also act as a "crucible in which inter-subgroup differences are sharpened" (Hogg 2006 p.123) Thus, due to the importance of these studies in formulating the basis of this research and highlighting the pertinent effect of SIT within corporate governance research, it is crucial to discuss their social identity construction, effects, and findings in detail.

One of the important studies that examined the board effectiveness using the concept of SIT is that of Hillman et al. (2008). By adopting identity theory and SIT with the literature on board monitoring and resource provision, the study investigates how directors' multiple identities affect their behaviour. As argued by Hillman et al. (2008), if people's identities affect their behaviour, directors' identities are also expected to affect board tasks and functions. Specifically, they suggest that the strength of a director's identification with the organisation, customers, or suppliers may positively impact his/her monitoring and resource provision roles. Following in the footsteps of Hilman et al. (2008), Melkumov et al. (2015) have also explored the relationship between directors' social identification and board tasks, in Finnish corporate boards, by applying a social identity perspective. The study corroborates the theoretical proposition of Hilman et al. (2008) by demonstrating that, the more directors identify with the organisation, the greater the likelihood that they will contribute to its success. The findings are thus consistent with those of Hilman et al. (2008), which posit and empirically find that organisation identification positively affects almost all board functions studied.

Although these studies have agreed about the beneficial effects of directors' organisation identification, Veltrop et al. (2018), in their study of the relationship between tenure and outside director task involvement, argue that organisational identification reduces directors' tendency to independently monitor, evaluate, and advise senior management. Using a sample of Dutch corporate boards, Veltrop et al.

(2018) suggest that outside directors are less likely to question and oversee the prevailing course of actions or to independently evaluate senior management strategic decision-making due to the strong social identification with the organisation. Thus, in the view of this study, the application of SIT in understanding director task involvement and effectiveness is comprehensive, but yet more complex than generally anticipated.

Apart from the above studies, there is a strand of literature that examines the genders' social identity and broad gender diversity through the lens of SIT. One such study is that of Terjesen and Sealy (2016), who have reviewed 120 articles and other publications concerning confliction tensions of board gender quotas through four different theoretical perspectives including SIT. In their review study, they suggest gender is now widely accepted as "socially constructed" (Terjesen and Sealy 2016, p.32) and, with growing numbers of women in managerial and board positions, future research needs to combine women's social identity perspective and other illuminating theoretical perspectives in gaining richer understanding on corporate board diversity and quotas. The latest study which has built upon SIT and focused on women's social identity is that of Chen et al. (2016), who have examined the effect of female board representation on the firm-level strategic level. SIT establishes that individuals respond differently to in-group members than to out-group members through in-group favouritism and out-group derogation (Hewston et al. 2002). In line with this premise, Chen et al. (2016) propose that the out-group members such as women on boards are more prompt to perceive such biases as identity threats, which in turn makes them be more competitive in interactions with the in-group members, and thus boards with one or more female directors are more likely to interact differently from comparable all-male boards. In this study, they also argue that the greater female board representation is linked with more inclusive board-level decision-making, which in turn can be linked with a more in-depth assessment of major strategic proposals.

Previous studies have also examined the effect of family members' identification on corporate and board behaviour. One of these studies was conducted by Deephouse and Jaszkiewicz (2013), who examined the effect of family members as one of the salient social identities on corporate reputation. According to Tajfel (1982), social identification with a group entails individuals not only being conscious of their group members but also valuing and being emotionally invested in the group. Therefore, in

a similar vein, Deephouse and Jaszkiewicz (2013) suggest that family members are more conscious, value, and emotionally invested in a family firm than non-family members are in family or non-family firms. Using an SIT to formulate the research hypotheses, they suggest that family members' heightened identification with their family firm empowers their involvement in organisational decision-making as well as motivates them to pursue a favourable reputation because it contributes to their socioemotional wealth.

In a more recent study, Suess-Reyes (2017) also provides a fresh perspective on family business governance by employing SIT as an alternative to the dominant agency theory. As emphasised by Whetten et al. (2014, p.480), SIT contributes a manner of capturing and explaining "the meaning of structures of the family and business component of a 'family business'". Moreover, the business family identity is an arrangement of realistic sense for the family, "more or less shared conceptions of 'who we are'" (Whetten et al. 2014, p.483). Using a large Australian dataset from a survey, Suess-Reyes (2017) exhibits that the business family's identity is positively associated with the transgenerational orientation of the business.

Most of the reviewed studies have examined the influence of overt salient identity to compliment the SIT within corporate governance issues; limited attention has been given to the construction of ascribed, innate identity or obscure identity. In a recent study, Zhang et al. (2020) fill the gap by suggesting that innate characteristics such as surnames can also be an important basis of self-identity and people's social identity. As Chinese people with the same surname generally reflect themselves and are convinced that they are from the same ancestor (Jacobs 1979; Langenburg 2007), Zhang et al. (2020) argue that this group of people also categorise and identify themselves into the same social group due to the ancestral relationship. Using a large sample of listed firms and directors in China, they find that the CEO-board surname ties increase agency costs, implying that directors tend to act as a social group when they share the same surname with the CEO.

The study provides a significant example to investigate the relationship between directors' social and economic roles through the lens of SIT, which is also closely related to our study. Using a shared surname to construct a shared social identity, Zhang et al.'s (2020) analysis, however, does not take account of the cultural group,

which can also develop and form group identity, which could also lead to in-group favouritism. Since culture is one of the salient and important identities which powerfully guides an individual's decisions, preferences, and behaviour (North 1990), thus, we fill the current research gap by proposing that cultural identity among directors and managers may also influence corporate and governance outcomes. In suggesting that cultural similarity is in-group favouritism, our study is closely related to the study of Shi and Tang (2015), who examined the effect of national cultural similarity between partner firms. However, their study relies heavily on the national culture, rather than individual culture, which conflicts with our study. Thus, we aim to shed valuable insights into the effect of individual or corporate actors' cultural identity within corporate boards, rather than the national culture across firms, on corporate value and board effectiveness via the lens of SIT.

2.3.5 Ties that bind: Implications of cultural similarity

Culture is an important defining feature of people's lives and plays a key role in influencing and shaping their ways of living, thinking, and socialising. In general, people with similar cultural values and backgrounds exhibit similar preferences, behaviours, and perceptions. Cultural similarity refers to the sharing of a common identity, and to the feeling of belonging to the same group, as well as to the degree of affinity between two people (Tajfel and Turner 1986). Due to the shared and common cultural values and attributes, research has also revealed that culturally similar individuals are more likely to be associates than are individuals who are culturally different (Byrne 1971; Kandel 1978; Leszczensky and Pink 2015), which is in line with the argument of McPherson et al.'s (2001) homophily theory. In general, the similarity in cultural values has considerable implications and influences for people.

First, the cultural similarity or familiarity between individuals forms an invisible bond, which can tie them together and establish a basic social network among people. According to Abdullah (1996, p.3), the culture of a society is the "glue that holds its member together through a common language, dressing, food, religion, beliefs, aspirations, and challenges". The subtle bond and shared social cues arising from cultural similarity, in turn, provide an advantage for more effective communication and expedite information flow between individuals. Members of a culture commonly share a common key for transmitting and interpreting their social environments, which

establishes rules for governing the interactions that are exclusive to them (Craig and Douglas 2006). As a result, the communication and interactions between the members are more effective, empathetic, and productive, which could also inhibit the possibility of information asymmetries between them. The cultural ties between individuals could also foster mutual support and facilitate trust creation among them due to their similar values and background. As argued by Earle and Cvetkovich (1995), people base their trust judgments on whether the other person is seen as having similar values. People from similar cultures more fluently perceive and interpret thrust-relevant signals, symbols, and patterns within their cultural sphere (Child and Mollering 2003). As a result, the trust formation between them consequently facilitates mutual understanding and emotional support among the members of the group (Nilsson 2019).

While cultural similarity facilitates better connection, communication, and trust between actors, the effects of cultural ties derived from the shared cultural values and backgrounds are not inherently positive. Second, as cultural ties are a vital basis of self-identity and social identity for people, they can give rise to in-group favouritism, which refers to in-group members extending preference and favour to each other over the out-group members in terms of behaviours, attitudes, preference, or perception (Turner et al. 1979; Hewstone et al. 2002). People with the same culture always consider themselves as in-group members and are believed to have the same group identity (Cokley 2007; Casey-Cannon et al. 2011). However, since the perpetuation of the in-group identity is vital to people's self-esteem, the need to accomplish positive group distinctiveness encourages people to compare their in-group with the out-group and to perceive the in-group as preferable (Brewer and Brown 1998). Furthermore, people tend to provide and allocate more resources towards in-group members, and positively support the thoughts and suggestions of in-group members but feel uncomfortable around, or merely avoid, out-group members (Yzerbyt and Demoulin 2010). As a result, this could lead to and provoke a pessimistic view of intergroup harmony (Tajfel 1982), negative stereotypes (Horwitz and Rabbie 1982), social distance (Sunar 1978; Smith 1983), discrimination or bias (Turner 1984), or prejudice (Masson and Verkuyten 1993) towards people with a dissimilar group such as a different cultural group (i.e., the out-group). For instance, in their analysis of inter-ethnic group hostilities, Tzeng and Jackson (1994) found that individuals with high in-group bias were significantly more negative towards members of other ethnic groups

in terms of their attitudes, behaviours, and cognitive judgments in many social settings. Similarly, Lee (1993) also found consistent results by providing evidence that Chinese Americans and Black Americans judge their in-group more positively than their out-group.

Third, the cultural ties between individuals could also establish significant social networks, which are among the important channels in gaining social capital through the virtue of membership. In his first systematic analyses of social capital, Bourdieu (1986) defined social capital as "the aggregate of the actual or potential resources which are linked to possession of a durable network of more or less institutionalised relationships of mutual acquaintance or recognition" (Bourdieu 1986, p.248). Various scholars interested in network relationships have recognised the value relevance of social capital to the network social processes and social outcomes (Burt 2000; Lee et al. 2001; Adler and Kwon 2002; Inkpen and Tsang 2005). Indeed, these scholars have shown and drawn a consensus that social capital provides several benefits that include privileged access to valuable resources such as knowledge, information, opportunities, and enhanced understanding of the network norms. Due to the shared norm, values, and beliefs, individuals from similar cultural backgrounds gain 'same-culture advantage', which in turn facilitates social trust and social capital among them. Hence, the members of the cultural group could benefit from the privileged access to valuable resources, preferential opportunities, and shared unique information, which is important to advance their status attainment as well as to reinforce and maintain group cohesion within-group ties.

Fourth, cultural ties have a significant impact on people, especially those in diverse and multicultural populations. In a multiculturalism setting, people tend to identify themselves and others as belonging to a certain cultural group (i.e., ethnic/racial/religious group) and emphasise category salience, membership, group identity, self-segregation, and ethnocentrism. For example, in a multiracial and cultural American setting (i.e., White, Black and Asian), studies have found that people with high in-group identity have different perceptions towards members of other or different ethnic groups in terms of their attitudes, behaviours, and cognitive judgments relating to several social matters (Tzeng and Jackson 1994). Furthermore, studies have also revealed that the highly identified majority members support intergroup relations more when their in-group's interests, status, or core values are at

stake (Morrison et al. 2009; Morrison and Ybarra 2009). The majority group members and particularly high-identifiers are more likely to ratify the ideology that promotes the maintenance of their cultural identity, status, and power position in society. Although a multiculturalism setting theoretically promotes cultural harmonisation and acceptance of out-group members, there can be situations in which it serves more the interests of the majority group in the population (Verkuyten 2013; Ng Tseung-Wong and Verkuyten 2018). For instance, in a multicultural nation like Malaysia, the majority ethnic group (i.e., Malay) receives more advantages and privileges than other ethnic groups (Noor and Leong 2013). Meanwhile, in Japan, people tend to accept the 'otherness' of ethnic minorities while still validating the right to preserve the original Japanese culture (Nagayoshi 2011) Thus, the implications of cultural ties are more ubiquitous and prevalent in a multicultural context, where we can expect more association between cultural/ethnic identification and in-group favouritism and intergroup bias.

Due to the significant effect of cultural similarity in reinforcing the bond and ties between cultural members and group identity, a large and growing body of literature has investigated how cultural similarity affects corporate and economic outcomes. Most of this literature has employed various variables to proxy cultural ties, such as common language, religion, ethnicity, or national culture (Boisso and Ferrantino 1997; Melitz 2008; Guiso et al. 2009; Shi and Tang 2015; Fisman et al. 2017). For example, Guiso et al. (2009) use religious and ethnic similarities as measurements for cultural similarity. They find that cultural similarity reinforces mutual trust, minimises transaction costs, and lubricates economic exchange, which could be evidenced in increased cross-border trade. Similarly, using religious similarity and ethnic similarity to proxy for cross-regional cultural similarity in the US, Shi and Tang (2015) find that cultural similarity facilitates interstate alliance activities between US states. Meanwhile, Ahern et al. (2015) find that national cultural similarity promotes cross-border mergers and acquisitions and reveal that investors react more positively towards such economic activity announcements by firms with a similar national culture than those by firms with different national cultures. In a more recent study, Hegde and Tumlinson (2018) find that venture capitalists are prone to invest in companies that are ethnically similar to themselves. The shared cultural values and backgrounds between individuals may motivate them to form group identity and

memberships, which in turn, increase the in-the presence of group favouritism and inter-group bias.

Although most of these studies had documented the significant impact of cultural similarity on various economic exchanges and corporate decisions, there is little direct evidence in corporate governance of the ways through which culture affects interactions between the key corporate governance actors, especially in the dyad of CEO and board of directors. In this respect, we postulate that cultural similarity between CEO and board of directors helps form a social tie between these two parties, and therefore our study aims to highlight the implications of such ties on firm value and governance outcomes.

2.4 The importance of culture for finance and corporate governance

What is culture? Notwithstanding the vast and ambiguous definitions of culture, most scholars, especially in the field of cross-cultural and organisational studies, have religiously relied on Geert Hofstede's definition of culture. In his seminal study, *Culture's Consequences,* Hofstede (2001, p.36) defines culture as "the collective programming of the mind distinguishing the members of one group or category of people from others". Meanwhile, North (1990, p.37) classifies culture as providing a "framework for encoding and interpreting the information that senses are presenting to the brain". In a more recent study, Guiso et al. (2006, p.23) described culture as "those customary beliefs and values that ethnic, religious and social groups transmit fairly unchanged from generation to generation". Observing these seminal definitions together, it is clear that culture encompasses an abiding set of beliefs or values that influences individuals' decisions, preferences, perceptions, behaviours, and interactions with others. Indeed, culture results from and influences behaviours and values. Thus, it is therefore more likely to impact a country's political rules, legal system and norms, labour market, capital market, corporate objectives and values, and consequently corporate finance and governance (Daniel et al. 2012). It is interesting to study the effect of cultural factors on finance and corporate governance issues as, unlike rules and laws that change over time and can be imposed externally, cultural values are deeply rooted and slow-moving (Williamson 2000; Tabellini 2008; Guiso et al. 2006, 2015). In turn, these cultural attributes may strongly influence individual,

society, and country as well as corporate decisions (Guiso et al. 2015). Moreover, by applying the cultural features to a financial context, important insights that may not be observed if using the traditional view of finance can be grasped and broadened. The business and corporate world is not restricted to functional areas; it is an integrated whole. Thus, culture may be the best direction to bridge disciplines to study the integrative reality of business and corporate practices.

2.4.1 The importance of culture for finance

In fact, there have been a number of studies investigating the effects of culture on financial and corporate practices. **Table 2.2** summarises the empirical studies of culture in finance. Amongst the earliest and impactful studies of culture in finance is that of Grinblatt and Keloharju (2001). Using Finnish firms as a study sample, the study reveals that investors are more prone to hold, buy, and sell the stocks of firms that are geographically proximate to the investor, that communicate in the investor's native language, and that have CEOs of similar cultural background. This study highlights the significance of familiarity in language, culture, and distance in explaining an investor's preference for certain firms. Apart from being the earliest study of culture in finance, this study has also initiated a unique and novel dataset, which encompasses language and cultural origin in measuring culture. As a matter of fact, numerous early studies on the impact of culture in finance have employed special or unique datasets rather than national culture dimensions in quantifying culture. Such studies also include Stulz and Williamson (2003) and Guiso et al. (2009), who have used religion and trust respectively as cultural attributes. Utilising cross-country religion in explaining why legal protections for shareholders and creditors differ across countries, Stulz and Williamson (2003) document that mostly Catholic countries protect creditors and shareholders less effectively than other countries. Meanwhile, Guiso et al. (2009) employed bilateral trust data as a cultural trait for stock market participation, documenting that a lower level of bilateral trust between countries leads to reduced trade and portfolio investment as well as direct investment.

While the breadth of cross-cultural studies has widely implemented the national cultural measures by Hofstede in explaining the effect of culture, research on culture in the area of finance has not been left behind in employing the prominent cultural measures. Although the earliest study in finance to employ the measure was initiated

a decade ago, numerous studies have progressively emerged and been published since then. The earliest and most well-cited study of culture in finance that has well-utilised the influential Hofstede measure is that of Chui et al. (2010). By focusing on Hofstede's (2001) 'individualism' index to measure cross-country cultural differences, this study investigates how cultural differences inform the returns of momentum strategies. Arguing that individualism is likely to be linked with overconfidence and attribution bias, Chui et al. (2010) show that individualism is positively associated with trading volume and volatility as well as with the magnitude of momentum profits. Thus, it has concurred that culture affects investor and stock price behaviour. This notion is also supported by a more recent study, by Eun et al. (2015), who demonstrate that countries that are culturally tighter and less individualistic have higher stock price co-movements. The results suggest that cultural differences indeed influence investor behaviour and decisions in the stock market. Consistent with the notion, the study also finds higher stock price synchronicity in countries with a tight and collectivistic culture. Further, apart from contributing to culture and finance literature, this study has also made a fascinating extension from the prior study by incorporating Hofstede's cultural dimension and including other cultural dimensions (tightness versus looseness) which were introduced by Pelto (1968) and Triandis (1989).

Several important studies have examined the effect of culture on financial policy and corporate financing choices. For example, Shao et al. (2010) show the effect of culture on firms' choice of dividend policy. Using Schwartz's national culture dimension, they find that conservatism is positively associated while mastery is negatively associated with dividend pay-outs. In a more recent study, Zheng et al. (2012) examined the important role of national culture in determining corporate debt maturity choice. Using Hofstede's cultural dimensions as proxies for culture, they find evidence that these cultural dimensions explain cross-country variations in the maturity of corporate debt. Meanwhile, Lievenbrück and Schmid (2014) find that culture influences the firm's decision to hedge. In a similar vein, Boubakri and Saffar (2016) provide evidence that culture directly affects the ability of firms to grow by documenting that Hofstede's cultural dimensions (i.e., individualism, masculinity, uncertainty avoidance, and power distance) affect firms' ability to overcome financial constraints. Similarly, El Ghoul and Zheng (2016) also consider the effect of culture on corporate financial decision-making by showing evidence that national culture

affects yet another firm financial decision, namely, trade credit. Apart from contributing to corporate policy and decisions, culture has also been considered important to another aspect of financial decisions, namely, corporate investment. As matter of fact, Li et al. (2013) have provided evidence that national culture influences corporate risk-taking through risky corporate decision-making and formal institutional developments. Using egalitarianism as a cultural dimension, Siegel et al. (2011) find that there is a strong negative impact of egalitarianism distance on international investment flows. In the same vein, Shao et al. (2013) find that culture affects corporate investment by exploring the relationship between individualism and types of corporate investment. They reveal that firms in individualistic countries invest more in long-term than in short-term assets. Together, these studies have shown that culture plays an important role in financial corporate policy and decisions.

Apart from highlighting the role of the cultural dimension, prior studies in finance have also documented the effects of cultural distance and familiarity on corporate decision-making and foreign investments. One of the earliest studies of cultural distance on finance is that of Beugelsdijk and Frijns (2010), who argue that cultural distance between two markets plays a key role in illuminating the foreign bias. This study finds that culturally distant country pairs invest less in each other than do culturally closer countries. A similar phenomenon can be found in Grinblatt and Keloharju (2001), who find that Finnish investors prefer stocks of firms from a similar culture as proxied by language. Similarly, Aggarwal et al. (2012) show that the different dimensions of cultural distance co-operate with the geographic distance affect and determine cross-country foreign portfolio investments. As justified by Karolyi (2016), cultural distance indeed has strong statistical powers in explaining foreign investment bias. Meanwhile, Ahern et al. (2015) highlight the role of cultural differences in cross-border mergers. Using a large sample of 52 countries between 1991 and 2008, they discover strong evidence that differences in national culture decrease the volume of cross-border mergers. The negative effect of cultural distance on the financial outcome is also supported by Lim et al. (2016) by arguing that cultural differences add constraints in post-deal integrations and reduce the expected synergy gains. Meanwhile, Giannetti and Yafeh (2012) examined whether cultural differences between professional decision-makers influence financial contracts. Using a large sample of international syndicated bank loans, they show that the more culturally

distant lead banks give borrowers smaller loans at a higher interest rate and are more likely to entail third party-guarantees. In the case of executive compensation contracts, Bryan et al. (2015) find that the cultural distances and differences have more potential to affect compensation structures across countries. Although these studies highlight the role of cultural distance, there is also a strand of literature that illuminates the role of cultural similarity as in-group favouritism. Such literature includes Shi and Tang (2015), who uses cross-regional religions and ethnic similarity as proxies for cultural heterogeneity in the US and find that the cultural similarity increases the volume of interstate strategic alliance.

Thus, based on the brief overview of the literature, there are important facts that are worth highlighting. First, although prior studies have examined the influence of culture in various aspects and different angles of financial decisions and corporate policies, their results are mostly consistent in justifying that culture does play a significant role in explaining such decisions. Second, most of the contributions have been published since the 2000s and the area is currently burgeoning, making this area topical in implying the importance of culture in finance research. Third, more of the studies cited above rely on the cultural dimensions of Hofstede. If not Hofstede, we can see that scholars use the dimensions of Schwartz or the World Values Survey in the main analysis or as a robustness test. Indeed, there are very limited studies that have employed different types of cultural measurement using unique or special data. Fourth, the earliest studies of culture within the finance area have mostly ignored or suffered in dealing with the problem of endogeneity (Aggarwal et al. 2016). Since culture can be related to both observed and unobserved variables, ignoring endogeneity issues might bring the results of previous studies into question. Only a few or recent studies have addressed the endogeneity problem by using various techniques such as the instrumental variables approach.

2.4.2 The importance of culture for corporate governance

While the extant literature acknowledges the influence of culture on shaping corporate and financial decisions, the effect of culture has also been ubiquitous in the area of corporate governance. As argued by Hofstede (1991), the values and organisational structure of corporations are a manifestation of a national culture in which that organisation functions. Moreover, institutional theory expects that organisations

conditionally rely upon their institutional environment, which also consists of the culture in which they function, and that corporate structures and models are derived from the institutional norms reflected in a particular society (Meyer and Rowan 1977; Williamson 2000). Such particular norms can be mainly expected, or established by public opinion, regulatory obligations, or legal system (Starbuck 1976). Thus, these norms not only involve normative rules and obligations, but also the shared values and beliefs that contribute to the culture of a society. Since culture, as a mixture of beliefs and values, is one of the ultimate institutional forces of any society, it is expected that organisational structure, objectives, and practices are strongly manifested by the prevailing cultural values found in that society in which they are developed. Indeed, prior studies have also supported the notion by indicating how differences in the institutional environment, as well as country characteristics, are the important basis for divergences in corporate governance codes and practices (Doidge et al. 2007; Aguilera and Jackson 2010). **Table 2.3** summarises the empirical studies of culture in corporate governance.

The extant studies about the influence of culture on corporate governance practices have mainly taken place using a cross-country sample. For example, Clement et al. (2003) examined how the differences in culture and corporate governance explain the forecast accuracy. Using a sample across 24 different countries, this study finds that the significance of experience and employer is subject to the type of culture and corporate governance of the country. Meanwhile, Tosi and Greckhamer (2004) use data from 23 countries to investigate whether cultural values are associated with different elements of CEO compensation in different countries. They find that all of the elements of CEO compensation are related to power distance, one of Hofstede's cultural dimensions. Further, they also find that total compensation and the ratio of variable to total pay are associated with individualism, which is another of Hofstede's cultural dimensions. In this study, they also highlight that the compensation structure of a firm is not only manifested from an organisation's values but also from the deeper social values that may differ across countries. Thus, this study shows how important it is to address cross-cultural differences in explaining the role of cultural values in CEO compensation as well as other corporate governance practices and in attempting to gain a deeper understanding of CEO compensation in the context of other cultures.

Meanwhile, some cross-country studies in the area of corporate governance have also emphasised the effect of culture on the dimensions of corporate governance such as board composition, size, independence, and structures. Such studies include Li and Harrison (2008a) and Li and Harrison (2008b), who use data on 15 industrial countries and explore how national culture influences the size, composition, and leadership structure of the corporate boards. These studies find that corporations based in a high-power distance society are more prone to have a single leader as both chair and CEO and fewer inside directors, while corporations based in a high individualistic society have smaller boards, more outside directors on their boards, and consolidated leadership positions. Meanwhile, more masculine corporations tend to have consolidated leadership positions and fewer outside directors. The studies also find that firms with a higher level of uncertainty avoidance tend to have more separation between CEO and board chair position and also more outside directors.

Using 32 countries to examine the implication of culture on the level of female representation on corporate boards, Carrasco et al. (2015) find that power distance and masculinity cultural dimension are negatively associated with the percentage of women on boards. Another important – and the latest – study to examine the association between national culture and corporate governance practices is that of Humphries and Whelan (2017). This study finds a significant relationship between national culture and four governance variables (i.e., board independence, gender composition, board leadership, and meeting frequency. Thus, the findings of prior studies confirm that culture, in general, has important implications for corporate governance elements, especially with regard to board and leadership structure. Indeed, these governance structures have been conditioned and modelled upon informal institutions, especially the cultural characteristics of the society.

Apart from the above studies, others have examined the effects of culture on corporate governance scores or ratings in explaining the quality of corporate governance practices. For instance, Chan and Cheung (2011) use seven corporate governance factors – discipline, transparency, independence, accountability, responsibility, fairness, and social awareness – in generating corporate governance scores and examine how Hofstede's cultural dimensions explain the variations levels of ethical sensitivity and corporate governance practices. Meanwhile, Daniel et al. (2012) employ Governance Metrics International (GMI), which provides corporate

governance ratings for individual companies, and investigate how both culture and institutions are linked to corporate governance practices. In more recent studies, Griffin et al. (2017a) and Griffin et al. (2017b) also use the same database in constructing corporate governance ratings for each firm year, and both studies find a significant association between culture and corporate governance ratings. Using a different measure of corporate governance, Duong et al. (2012) examine how culture influences cross-country variations in corporate governance practice by using the pillar score of the Corporate Governance Index (*G-Index*) obtained from the Datastream ASSET4 ESG databases. They find a robust and significant relationship between national culture and corporate governance after controlling for firm-level and country-level characteristics. Although prior studies have employed various corporate governance measures or indicators, the results are still similar and this confirms the importance of culture in corporate governance.

Even though cross-country studies are noteworthy in explaining the effect of culture on the cross-country variations in corporate governance practices, these studies have some overt limitations. They have often classified culture at a country level and measured it together with other national or institutional attributes such as legal, political, financial, or economic system. Thus, the cultural-specific effects may be difficult to observe and comprehend (Volonté 2015). In fact, prior studies have often viewed cultures as a national factor and intra-cultural heterogeneity is largely overlooked. As a result, numerous studies have investigated the influence of culture on corporate governance based on a single country, which allows us to understand the actual effect of culture on corporate governance practice. For instance, Buck and Shahrim (2005) investigate the effects of national culture on changes in regulatory and firm-level governance in Germany. Using Germany as a setting due to its distinctive characteristics instead of using an Anglo-American setting, this study demonstrates that national culture is associated with entire systems of corporate governance, especially stock market and welfare capitalism. In the context of Malaysian corporations, Haniffa and Cooke (2002) have argued that information disclosure practice, which is also one of the board's functions, is reflected due to cultural factors. The study utilises a Malaysian setting due to the country's unique multicultural society that has been divided based on ethnicity, religion, and language. In a different paper but a similar vein, Haniffa and Cooke (2005) have also employed the ethnic

background of directors and shareholders as a proxy for culture and examined the effects of culture and corporate governance on social disclosures. They find a significant association between corporate social disclosures and boards dominated by ethnic Malay directors.

Another important – and the latest – study to examine the effect of culture on corporate governance is that of Volonté (2015). Using the corporate landscape of Switzerland as the study sample, Volonté operationalises language (i.e., German and French) as well as religion (Roman Catholicism and Protestantism) as two proxies of culture. As a matter of fact, these proxies are well known to be very much a part of Switzerland's cultures and hierarchical structures, and therefore have a potential influence on corporate governance. In fact, culture is difficult to distinguish from other institutional forms within a country. Nevertheless, because the study is based on a single country, it benefits from the country's constant characteristics of legal origins and political systems, which enables the author to focus on the real effect of culture. This study finds that firms in Swiss-French areas and firms in Roman Catholic cantons are more prone to have a one-tier board and this shows that culture plays an important role in one of the corporate governance elements, which is board composition.

While prior studies above have used cultural dimension as the independent variables, Frijns et al. (2016) examine the role of cultural distance on a sample of UK firms. In particular, they investigate the effect of cultural diversity in corporate boards on firm performance. While many studies have observed the association between board diversity in terms of gender, education, and so forth, and firm performance, Frijns et al. (2016) distinguish their study by examining board diversity in terms of the distance between directors' cultural backgrounds. Furthermore, while most of the above studies have measured culture differences across countries or firms, this study contrarily measures cultural differences *within groups* (board), which is a novel concept in the culture and corporate governance literature. Using a sample of UK firms that consist of 95% of the market capitalisation of the London Stock Exchange between 2002 and 2014, this study finds that national cultural diversity negatively impacts firm performance as measured by Tobin's Q and return on assets. While this study explores the effect of diversity of directors' cultural background, there is also an important and most recent study that explores the effect of CEO's cultural background. In particular, Nguyen et al. (2018) explore how a CEO's cultural heritage and background affect

corporate outcomes. In order to identify the CEO's cultural heritage, they manually gather data on the country of origin of a CEO's ancestors from ancestry.com and they discover that banks led by CEOs who were children and grandchildren of immigrants have a greater performance when there is high industry competition.

Hence, based on the evidence in the extant literature about the role of culture in corporate governance research, we extend the previous research and explore the role of culture within corporate boards. In particular, we investigate whether culture plays a significant role in the relationship between CEO and board and how having a CEO and board from a similar cultural background affects firm performance and board monitoring. Our study is closely related to Frijns et al. (2016), who studied the effect of cultural differences within directors on boards. Instead of examining the effect of cultural diversity on firm performance, we extend and complement this line of research by showing evidence on how cultural ties between CEO and other directors on a board affect firm performance as well as board effectiveness. In fact, the cultural differences or similarities between this dyad (CEO-board) have not been considered in the corporate finance and corporate governance literature. Thus, we introduce a novel concept within these fields by measuring CEO-board cultural similarity to examine the impact of cultural factors in corporate boards on firm performance and the board's monitoring role.

Table 2. 2: Summary of empirical studies of culture in finance

Author	Title	Year	Country	Cultural dataset(s) used	Cultural variable used	Endogeneity tests	Main findings
Grinblatt and Keloharju	How distance, language, and culture influence stockholdings and trades	2001	Finland	Language and cultural origin	Cultural similarity	No explicit endogeneity tests	Investors are more likely to hold, buy, and sell the stocks of Finnish firms that are located close to the investor, that communicate in the investor's native tongue, and that have chief executives of the same cultural background.
Stulz and Williamson	Culture, openness and finance	2003	49 countries	Religion and language	Cultural differences	No explicit endogeneity tests	A country's principal religion predicts the cross-sectional variation in creditor rights better than a country's natural openness to international trade, its language, its income per capita, or the origin of its legal system. Catholic countries protect the rights of creditors less well than Protestant countries. A country's natural openness to international trade mitigates the influence of religion on creditor rights.
Guiso, Sapienza and Zingales	Cultural biases in economic exchanges	2009	EU countries	Bilateral trust data	Cultural distance (biases)	No explicit endogeneity tests	Lower bilateral trust leads to less trade between two countries, less portfolio investment, and less direct investment.
Chui, Titman, and Wei	Individualism and momentum around the world	2010	41 countries	Hofstede	Cultural dimensions	No explicit endogeneity tests	Individualism is positively associated with trading volume and volatility, as well as to the magnitude of momentum profits.
Shao. Kwok and Guedhami	National culture and dividend policy	2010	21 countries	Schwartz	Cultural dimensions	Yes	Conservatism is positively related and Mastery negatively related to dividend pay-outs.
Beugelsdijk and Frijns	A cultural explanation of the foreign bias in international asset allocation	2010	26 countries	Hofstede	Cultural distance	No explicit endogeneity tests	More uncertainty avoiding nations allocate less money abroad and more individualistic nations invest more abroad. Culturally distant country pairs invest less in each other than do countries that are culturally closer.

Siegel, Nicht and Schwatz	Egalitarianism and international investment	2011	55 countries	Schwartz	Cultural dimensions	No explicit endogeneity tests	Egalitarianism distance negatively affects flows of bonds, equities, syndicated loans, and M&A.
Aggarwal, Kearney, and Lucey	Gravity and culture in foreign portfolio investment	2012	174 countries	Hofstede	Cultural distance	No explicit endogeneity tests	Cross-border foreign portfolio investments (FPI) patterns are significantly determined by the cultural characteristics of both the originating and destination countries as well as by the cultural distance between them. Common language and religion between financial trading partners exerts significant positive effects on cross-border FPI holdings of both debt and equity.
Giannetti and Yafoh	Do cultural differences between contracting parties matter? Evidence from syndicated bank loans	2012	70 countries	WVS	Cultural distance	No explicit endogeneity tests	More culturally distant lead banks offer borrowers smaller loans at a higher interest rate and are more likely to require third-party guarantees.
Zheng, El Ghoul, Guedhami and Kwok	National culture and corporate debt maturity	2012	40 countries	Hofstede with Schwartz for robustness	Cultural dimensions	No explicit endogeneity tests	Firms located in countries with high uncertainty avoidance, high collectivism, high power distance, and high masculinity tend to use more short-term debt.
Li, Griffin, Yue and Zhao	How does culture influence corporate risk-taking?	2013	35 countries	Hofstede	Cultural dimensions	Yes	Individualism has a positive and significant association, whereas uncertainty avoidance and harmony have negative and significant associations, with corporate risk-taking. Greater earnings discretion strengthens and larger firm size weakens the association of culture with corporate risk-taking.
Shao, Kwok and Zhang	National culture and corporate investment	2013	44 countries	Hofstede	Cultural dimensions	Yes	Firms in individualistic countries invest more in long-term (risky) than in short-term (safe) assets and the effect of individualism on long-term investment hinges on R&D: firms in individualistic countries invest more in R&D projects but not more in physical assets.

Lievenbrück and Schmid	Why do firms (not) hedge? — Novel evidence on cultural influence	2014	Over 500 countries	Hofstede	Cultural dimensions	Yes	Companies in long-term oriented cultures are less likely to hedge and they hedge a lower fraction of their exposure.
Shi and Tang	Cultural similarity as in-group favouritism: The impact of religious and ethnic similarities on alliance formation and announcement returns	2015	US	Religion and ethnic origin data	Cultural similarity	Yes	The cross-regional religious similarity and ethnic similarity in the US positively affect the volume of interstate alliance activities, but are negatively associated with combined alliance announcement returns of partner firms.
Eun, Wang, and Xiao	Culture and R2	2015	47 countries	Hofstede	Cultural dimensions	Yes	Countries that are culturally tighter and less individualistic have higher stock price co-movements.
Ahern, Daminelli and Fracassi	Lost in translation? The effect of cultural values on mergers around the world	2015	52 countries	WVS	Cultural distance	Yes	The volume of cross-border mergers is lower when countries are more culturally distant. In addition, greater cultural distance in trust and individualism leads to lower combined announcement returns.
Bryan, Nash and Patel	The effect of cultural distance on contracting decisions: The case of executive compensation	2015	39 countries	Hofstede	Cultural distance	Yes	The differences in Individualism and differences in Uncertainty Avoidance are significantly related to variation in compensation structure.
Boubakri and Saffar	Culture and externally financed firm growth	2016	56 countries	Hofstede	Cultural dimensions	Yes	Cultural dimensions of individualism, masculinity, uncertainty avoidance, and power distance affect a firm's ability to overcome financial constraints, with individualism exhibiting a strong robust impact compared to the other dimensions.
El Ghoul and Zheng	Trade credit provision and national culture	2016	49 countries	Hofstede	Cultural dimensions	Yes	Suppliers located in countries with higher collectivism, power distance, uncertainty avoidance, and masculinity scores tend to offer more trade credit to their customers.
Lim, Makhija and Shenkar	The asymmetric relationship between national cultural distance and target premiums in cross-border M&A	2016	US	Hofstede and GLOBE	Cultural distance	No explicit endogeneity tests	There is a strong negative association between cultural distance and premiums when US firms bid for foreign targets; no such negative association is observed when foreign bidders evaluate US targets.

Karoyli	The gravity of culture for finance	2016	57 countries	Hofstede, WVS and GLOBE	Cultural distance	No explicit endogeneity tests	Cultural distance has strong statistical powers in explaining foreign investment bias.

Source: Compiled by the researcher

Table 2. 3: Summary of empirical studies of culture in corporate governance

Author	Title	Year	Country	Cultural dataset(s) used	Cultural variable used	Endogeneity tests	Main findings
Haniffa and Cooke	Culture, corporate governance and disclosure in Malaysian corporations	2002	Malaysia	Hofstede, ethnicity and education	Cultural dimensions	No explicit endogeneity tests	Significant associations (at the 5% level) between two corporate governance variables (*viz* chair who is a non-executive director and domination of family members on boards) and the extent of voluntary disclosure. One cultural factor (proportion of Malay directors on the board) is significantly associated (at the 5% level) with the extent of voluntary disclosure.
Clement, Lees, Swanson	The influence of culture and corporate governance on the characteristics that distinguish superior analysts	2003	24 countries	Hofstede	Cultural dimension	No explicit endogeneity tests	Relative forecast accuracy is influenced by years of experience, size of the analyst's employer, and frequency of forecast issuance for many of these countries, and shows that the significance of experience and employer is conditional on the type of culture and corporate governance of the country.
Tosi and Greckhamer	Culture and CEO compensation	2004	23 countries	Hofstede	Cultural dimensions	No explicit endogeneity tests	All of the different dimensions of CEO pay were related to power distance, inferring that CEO pay in a culture is most reflective of the strength of the power structure in a society, and total compensation and the ratio of variable pay to total pay are related to individualism.
Haniffa and Cooke	The impact of culture and governance on corporate social reporting	2005	Malaysia	Ethnicity	Cultural dimension	No explicit endogeneity tests	There is a significant relationship between corporate social disclosure and boards dominated by Malay directors, boards dominated by executive directors, chair with multiple directorships, and foreign share ownership.

Buck and Shahrim	The translation of corporate governance changes across national cultures: the case of Germany	2005	Germany	Coevolutionary perspective	Cultural dimension	No explicit endogeneity tests	There is an association between national culture and entire systems of corporate governance, particularly stock market and welfare capitalism.
Li and Harrison	Corporate governance and national culture: a multi-country study	2008	15 countries	Hofstede	Cultural dimension	No explicit endogeneity tests	National cultures of the home countries of MNCs have powerful influences on their governance structures.
Li and Harrison	National culture and the composition and leadership structure of boards of directors	2008	15 countries	Hofstede	Cultural dimensions	No explicit endogeneity tests	The cultural dimensions of uncertainty avoidance, individualism/collectivism, masculinity/femininity, and power distance have significant power to predict the composition and leadership structure of corporate boards in different countries.
Daniel, Cieslewicz and Pourjalali	The impact of national economic culture and country level institutional environment on corporate governance practices	2011	40 countries	Hofstede	Cultural dimensions	No explicit endogeneity tests	There is a strong relationship between national cultures and corporate governance practices.
Chan and Cheung	Cultural dimensions, ethical sensitivity and corporate governance	2012	12 countries	Hofstede	Cultural dimensions	No explicit endogeneity tests	Hofstede's cultural dimensions can explain the differences in CG practices.
Carasco, Francoeur, Labelle, Laffarga, Ruiz-Barbadillo	Appointing women to boards: is there a cultural bias?	2015	32 countries	Hofstede	Cultural dimensions	No explicit endogeneity tests	Two cultural characteristics, as measured by the Hofstede (1980) dimensions, are associated with variations observed in the level of female representation on corporate boards.
Volonté	Culture and corporate governance: The influence of language and religion in Switzerland	2015	Switzerland	Language Religion	Cultural differences	No explicit endogeneity tests	Firms opt for board structures that correspond to their cultural identity. Board composition is influenced by language. Directors are active in firms where they share a common first language which is also the regional language of the corporation's headquarters.

Frijns, Dodd and Cimerova	The impact of board cultural diversity on firm performance	2016	UK	Hofstede with Schwartz and GLOBE for robustness	Cultural distance (diversity)	Yes	National cultural diversity in boards negatively affects firm performance measured by Tobin's Q and ROA.
Duong, Kang, Salter	National culture and corporate governance	2016	41 countries	Hofstede	Cultural dimension	Yes	There is a significant relation between national culture and corporate governance, controlling for firm-level and country-level characteristics, including measures of formal institutions and economic development.
Griffin, Guedhami, Li and Shao	National culture: The missing country-level determinant of corporate governance	2017	41 countries	Hofstede	Cultural dimension	Yes	Hofstede's individualism dimension is positively associated with corporate governance practices such as transparent disclosure, equity-based pay, and board independence, whereas his uncertainty avoidance dimension is negatively associated with these corporate governance practices.
Griffin Guedhami, Kwok, Li and Shao	National culture and the value implication of corporate governance	2017	38 countries	Hofstede with Schwartz as robustness	Cultural dimension	Yes	National cultural dimension of individualism is positively associated with, whereas the national cultural dimension of uncertainty avoidance is negatively associated with, firm-level corporate governance scores.
Humphries and Whelan	National culture and corporate governance codes	2017	55 countries	Hofstede	Cultural dimension	No explicit endogeneity tests	Significant relationships between Hofstede's cultural dimensions and the four characteristics of corporate governance (gender composition, board independence, board leadership structure, and meeting frequency).
Nguyen, Hagendorff and Eshraghi	Does a CEO's cultural heritage affect performance under competitive pressure?	2018	US	Hofstede, Schwartz, Globe Project and WVS	Cultural heritage (background)	No explicit endogeneity tests	CEOs whose cultural heritage emphasises restraint, group-mindedness, and long-term orientation were safer, more cost efficient and, as a result, more likely to outperform under pressure.

Source: Compiled by the researcher

2.4.3 Cultural datasets and the potential fragility of cultural measurement

In cross-country studies of the effect of culture on finance and corporate governance, most scholars have relied heavily on national cultural datasets by Hofstede, Schwartz, GLOBE, and the World Values Survey (WVS). **Table 2.4** provides a summary of these cultural datasets. Among these four datasets, Hofstede's is the earliest, most influential, and most widely cited. By far, Hofstede's cultural dimension framework is perhaps the most comprehensive framework of national culture and is verified by its cumulative influence on business studies. The framework constitutes a simple, practical, replicable, and useful way to incorporate culture into studies. Moreover, it facilitates cultural measurements that display strong and robust explanatory power, with the observed coefficients being both statistically and economically significant (Aggarwal et al. 2016). For example, Hofstede's individualism-collectivism dimension (IND) has been utilised frequently as a strong predictor of various financial and corporate outcomes, with the results continuing to hold and be robust even after controlling and taking into account country-level factors such as economic level, legal, and investor protections (Aggarwal et al. 2016). Nevertheless, such ground-breaking datasets do not escape several caveats and criticisms.

As a matter of fact, culture itself is "fuzzy and difficult to define and construct" (Triandis et al. 1986, p.258), thereby it is difficult to measure due to its subjectivity and ambiguity. Unlike accounting and stock market data, which are formed on frequently collected numerical observations, cultural data are commonly gathered based on the subjective answers from the participants (Aggarwal et al. 2016). In fact, some researchers argue that a survey is not a suitable instrument for precisely determining and measuring cultural values and attributes. Take Hofstede's (2001) cultural dimensions as an example. The cultural dataset was collected from 1967 to 1973 and is ageing and old, thereby researchers criticise the relevancy of the data to be any of modern value given today's volatile business environments. However, Hofstede argues that recent and growing publications which replicated the use of his cultural dataset show that culture will not change overnight (Hofstede 1998). Another important argument was highlighted by prior studies which famously criticise that Hofstede's study of the subsidiaries of a single company (i.e., IBM) may not reflect information about entire national cultures (Myers and Tan 2002; Baskerville 2003). Thus, the validity and reliability of this particular cultural data in capturing all the

cultural values have been questioned. **Table 2.5** summarises the main criticisms of Hofstede's cultural dataset based on Baskerville (2003), Myers and Tan (2002), and McSweeney's (2002a, 2002b) analyses.

Despite being the earliest and most widely cited cultural measure, Hofstede's cultural dataset has been repeatedly criticised and challenged, mostly due to its use of national borders to capture cultural differences. His influential theory simply equates nation-states with cultures. According to Hofstede (1991, p.12), nations are "the source of a considerable amount of common mental programming of their citizens", as nations with a long history have strong forces towards further integration. While, in fact, cultures do not equate with nations (Baskerville 2003) and are not necessarily bounded by borders (McSweeney 2000). Another important criticism is that Hofstede does not address the fact that many countries have different subcultures (Baskerville 2003; House et al. 2004). In fact, there is commonly more than one culture in one country. Thus, it may not be appropriate to associate the word culture with a nation as its domestic population is not always homogenous. This implies that nations are somewhat arbitrary political formations that are not necessarily formed along established cultural lines (Myers and Tan 2002; Baskerville 2003).

Therefore, this approach is certainly not relevant and is inadequate for a nation that has a multicultural society, such as Malaysia. As suggested by Baskerville-Morley (2005, p. 391), business studies need to acknowledge that a variety of behaviours and perceptions differ with the "ethnicity of participants, not political or national groupings". This ethnic identification by participants offers an informative and "valuable predictor of how shared cultural values will impact both individual and small-group behaviour" (Baskerville-Morley 2005, p.391). Therefore, reflecting on all of these criticisms and the fragility of the existing cultural datasets, we use the ethnic identity of participants (i.e., CEOs and board of directors) as the best cultural measurement in determining how the shared culture affects their roles and behaviours.

In summary, while there are some criticisms in utilising the existing cultural dataset as a measure of culture in explaining cross-border differences in financial and corporate decisions, cultural measures have been helping to shed light on other corporate decisions and behaviours for some considerable time and exhibit great probability to enhance our understanding of corporate and financial behaviours and

decisions as well. Nevertheless, as mentioned by McSweeney (2002, p. 113), "instead of seeking an explanation for assumed national uniformity from the conceptual lacuna that is the essentialist notion of national culture, we need to engage with and use theories of action which can cope with change, power, variety, multiple influences – including the non-national – and the complexity and situational variability of the individual subject". Therefore, researchers of cultural studies in finance as well as corporate governance need to take into account the critical debates in improving and determining the current cultural measurement to suit and incorporate with their studies.

Table 2. 4: Summary of main datasets of national culture

Datasets	Cultural dimensions	Years of data collection	Countries covered	Survey respondents	Remarks
Hofstede	Four main dimensions: individualism vs. collectivism; power distance; uncertainty avoidance; and masculinity vs. femininity. Later added long-term orientation and indulgence vs. restraint.	Mostly 1967 to 1973	Initially 40 countries; later extended to 50 countries	IBM employees	The most widely cited dataset on national culture. Recently, items from the World Values Survey were used to extend coverage to 93 countries.
Schwartz	Six value types: conservatism; intellectual and affective autonomy; hierarchy; mastery; egalitarian commitment; and harmony.	1990s	Initially 22 countries; later extended to 64 countries	Elementary school teachers and college students	The six value types can be consolidated into two broad dimensions: 1) autonomy vs. conservatism, and 2) hierarchy and mastery vs. egalitarian commitment.
GLOBE	Nine dimensions: assertiveness, institutional collectivism; in-group collectivism; future orientation; gender egalitarianism, humane orientation; performance orientation; power distance; and uncertainty avoidance.	1990s	62 countries	Middle managers	Each cultural dimension is further divided into a value score (i.e., desired practice) and a belief score (i.e., actual practice).
World Values Survey	An extensive questionnaire surveying people's values and beliefs towards politics, religion, family, the environment, etc.	Six waves since 1981; 7th wave (2017 to 2021) planned	Nearly 100 countries in recent waves	Sample from general population 18 years and older	No clearly consolidated cultural dimensions. But the survey is conducted every several years to detect the value changes.

Source: Aggarwal et al. (2016)

Table 2. 5: Summary of the main criticisms of Hofstede's cultural dataset based on Baskerville (2003), Myers and Tan (2002), and McSweeney's (2002a, 2002b) analyses.

List of criticisms	Authors
That the data which formed the basis of Hofstede's analysis was not collected with this in mind; was not representative of people in those countries	Myers & Tan, & Baskerville
That there is such a thing as 'national culture'. The problem with the unit of the analysis being a territorially unique nation-state	Myers & Tan, McSweeney, & Baskerville
Nation states are a relatively recent phenomenon	Myers & Tan
National states are dynamic, and older states have major changes in population and ethnic composition	Myers & Tan, McSweeney
Nation states do not each have their own single and distinct culture; many nation states have multiple ethnicities	Myers & Tan, Baskerville
Hofstede's view of culture is not supported from current anthropological perspectives; its foundations are no longer mainstream anthropology	Myers & Tan, Baskerville
The relationship between national cultural values and culturally-influenced work-related values; Hofstede credits national cultures with strong, or even absolute, causality	Myers & Tan, McSweeney
The simple model presented by Hofstede did not allow for the complex relationships between culture and economic indicators	Myers & Tan, Baskerville
That culture is not observable or recordable, but implicit, a type of mental programming	McSweeney, Baskerville
The claim of an immutability of cultures: that each has a discrete unique nucleus or core	McSweeney, Baskerville
That IBM has a single, uniform and monopolistic organisational culture	McSweeney, Baskerville
That national cultural 'sharedness' between individuals can be derived from a statistical averaging of heterogeneous components; a national norm	McSweeney
That the sample was only from IBM employees, with a single uniform organisational culture	Myers & Tan, McSweeney, Baskerville
That he had to assume a national uniformity of culture in order to find it	McSweeney

Source: Baskerville-Morley (2005)

2.4.4 Measuring CEO-board cultural similarity

After reflecting on the previous studies of culture and the fragility of the existing cultural measurements, this thesis uses the ethnic identity of participants (i.e., CEOs and board of directors) in determining how the shared culture affects their roles and behaviours. As observed by Baskerville-Morley (2005, p.391) in dealing with the limitations of the existing cultural measurements, research on business needs to concede that a variety of behaviours and perceptions differ with the "ethnicity of participants, not political or national groupings". Therefore, participants' ethnic identification may offer a more informative and "valuable predictor of how shared cultural values will impact both individual and small-group behaviour" (Baskerville-Morley 2005, p.391).

In particular, in constructing our measures of CEO-board cultural similarity, we use the CEO and other board of directors' ethnic identity as an indicator of their cultural values. In fact, ethnicity is not only a fundamental part of an individual's self-identity but is also one of the most eminent identity cues that can distinguish individuals (Cokley 2007; Higginbotham and Andersen 2012)[3]. Ethnic identity signifies "how individuals see themselves relative to their cultural beliefs, values, and behaviours" (Cokley 2007, p.225). Individuals from different ethnic origins own different attitudes, values, and norms that reflect their cultural heritage (Betancourt and Lopez 1993). In an analysis of the relationship between ethnicity and culture, Desmet et al. (2017) find that ethnic identity appears to be an important determinant of cultural norms, values, and preferences. Apart from influencing people's cultural beliefs and values, ethnicity may also influence the way board members interact and socialise. Therefore, in capturing the presence of CEO-board cultural similarity within a firm's corporate boards, the CEO's and other board of directors' ethnic identity has been used as an indicator of their cultural values.

In order to identify the ethnic origins of CEO and directors, we obtain their names from the Bloomberg database as well as from annual reports. The name-based

[3] In Malaysia, it is also considered as an "ascribed identity – one's [ethnicity] as a 'Malay', 'Chinese', 'Indian' or 'Other' (MCIO) is identified and determined at/by birth, inscribed on the birth certificate, and, from the age of 12, on the national identity card, and cannot be changed" (Gabriel 2015, p. 783).

ethnicity indication[4] is a relevant and sufficient approach to identify the ethnicity of the directors and CEOs, as the names of Malays, Chinese, Indians, and foreigners are very distinct. Our approach is similar to other existing studies in Malaysia that use names to identify ethnic origins (Yatim et al. 2006; Ahmad-Zaluki 2012; Gul et al. 2016). In this study, we classify the ethnicity of board members into four categories: Malay, Chinese, Indian, and Others. A director with a Muslim name with Arabic patronymics (either 'Binti' or 'Bin', which means 'daughter of' or 'Son of', respectively) is identified to be Malay, a director with a surname such as Tan, Lee, or Chan is considered to be Chinese, and directors with names such as Krishnan and Bala are recorded as Indians. The 'Others' ethnic category comprises non-Malaysian citizens or foreigners, regardless of their specific nationality. We also cross-validate our name-based ethnical classification procedure by examining facial images of the directors/CEOs from annual reports as well as obtaining information about their ethnicity from websites and newsletters.

Identification of ethnicity allows us to construct our key variable of interest, the cultural similarity between CEO and other board directors (***Cultural Similarity***), which is the proportion of directors on the firm's board that share a similar ethnicity to the CEO, i.e., the number of directors that share a similar ethnic background with the CEO/total number of directors.

2.5 Institutional background: Malaysia

2.5.1 Malaysia: Asia's ethnic and cultural melting pot

"*Malaysia is a nation of ethnics rather than a nation of citizens*"

(Ong 2009, p.476)

Malaysia is a nation situated in Southeast Asia, consisting of two distinct geographical regions divided by 640 miles of the South China Sea, with the Peninsular Malaysia to

[4] This view is also supported by Mateos (2007), who argues that the name-based ethnicity classification method presents a valid alternative technique for ascribing individuals to ethnic groups, when self-identification is not available.

the west and Malaysian Borneo to the East, which can be seen in **Figure 2.1**. Bordered by Brunei, Thailand, and Indonesia, and along with a heritage of diverse influences including a long period of British colonisation, Malaysia is one of the most multicultural nations in Southeast Asia (Webster 2010).

Figure 2. 1: Map of Malaysia

Source: Encyclopaedia Britannica Inc. (2009)

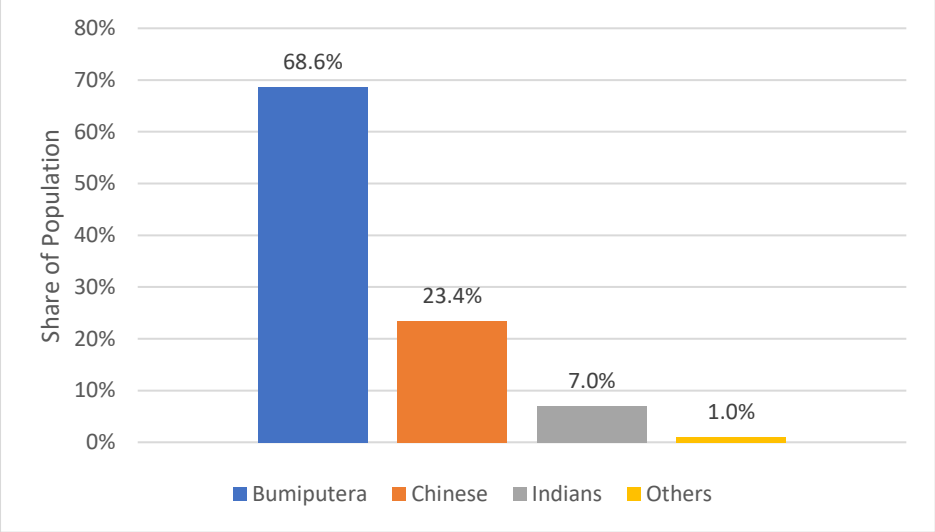
Unlike other Asian countries, Malaysia is not a nation that comprises a culture that is distinctly tied to one ethnicity, custom, or language. Due to its rich history, Malaysia has become a classic setting that signifies the coexistence of three clearly identified[5] major ethnic groups (i.e., the Malays, Chinese, and Indians) with distinct racial, linguistic, religious, and cultural identities (Abraham 1999; Haque 2003) and it has extensive state policies, rules, and regulations in various sectors to address important issues pertaining to the ethnicity (Haque 2003), as well as being an excellent platform to study cultural assumptions due to its ubiquitous diversity of cultures and ethnicity (Schermerhorn 1994, p.53). In Malaysia, ethnicity has been influential and prevalent in almost every dimension of life. As articulated by Crouch (2001, p.230), since the post-colonial period, most of the policy concerns in Malaysia have been influenced by

[5] In Malaysia, it is also considered as an ascribed identity – one's ethnicity as a 'Malay', 'Chinese', 'Indian' or 'Other' (MCIO) is identified and determined at/by birth, inscribed on the birth certificate, and, from the age of 12, on the national identity card, and cannot be changed (Gabriel 2015, p. 783).

ethnicity, including "language, education, government, employment, immigration, internal security, foreign policy, or virtually everything else".

Malaysia's population comprises three major ethnic groups, where the Bumiputera[6] (*sons of the soil*), which consists of the Malays and the indigenous people, is the largest group, consisting of more than half of the nation's population, followed by the Chinese, who represent about 23% of the population, whereas 7% are Indians and 1% percent are 'Others' (Department of Statistics Malaysia 2016). **Figure 2.2** shows the share of the population for each major ethnic group in Malaysia as of 2016.

Figure 2. 2: Share of the population by ethnicity in Malaysia as of 2016



Source: Department of Statistic Malaysia (2016)

Explaining the structure and nature of Malaysia's ethnic diversity and relations is impossible without adequately understanding Malaysian history (Kia Soong 1987; Abraham 1997; Munusamy 2012). Hence, the next section will discuss the history of Malaysia, particularly the emergence of a plural society and ethnic fissures.

2.5.2 A brief history of multiculturalism and ethnic faultline in Malaysia

Before the colonisation doctrine emerged in Asia, this part of Southeast Asia had always been known for its plurality in societies and ethnicities (Shamsul 1996). Due to its highly strategic geographical location between the Indian Ocean and South China

[6] In spite of the fact that the term *Bumiputera* consists of Malays and other indigenous groups, it is prevalent in Malaysia that the term is often used to refer to the Malays since they form the bulk of *Bumiputera* (Gomez 2002; Gul et al. 2016). Meanwhile, the indigenous people are commonly referred to by their tribal name such as Dayaks, Kadazan, or Orang Asli. Therefore, the words *Bumiputera* and Malays will be used interchangeably in this thesis unless otherwise stated.

Sea, Malaysia, which was previously known as Malaya, has long been the international meeting and trading hub for travellers from the West and the East (Mariappan 2002). During the middle and late 1400s, most of the area was occupied by the Malaccan Sultanate and it flourished to become one of the most powerful and wealthy kingdoms in the region with a wealth of resources. The thriving region then attracted the attention of the Portuguese in 1511, who were among the first European colonists in Malaya, followed by the Dutch in 1641 and later by the British in 1874 (Hirschman 1986). Moreover, there was also a short period of Japanese invasion and occupation from 1941 to 1945, then the country was later taken over and ruled by the British again (Hirschman 1986; Ibrahim et al. 2011). Although the Portuguese and Dutch colonisation periods witnessed some migratory and pluralism effects as before, it was the British rule that facilitated most of the changes that occurred in Malaysia, especially in social, political, and economic sectors (Hirschman 1986; Haque 2003).

In the early 19th century, the colonial economy of tin mining, sugar, and rubber plantation that flourished during the British colonisation period attracted large numbers of Chinese labourers and businessmen as well as Indian plantation labourers from their respective countries to Malaya to assist the British in the exploitation of resources in Malay states (Hirschman 1986, p.356; Cheah 2009, p.35; Khoo 2009, p.14) This major phenomenon of immigration strongly changed the demographic shape of Malayan society. By 1921, the number of immigrants had significantly eroded the majority of the Malay population (Mariappan 2002; Mohamad-Yusof et al. 2018). Furthermore, the introduction of the British '*divide and rule*' policy changed Malayan society into a classic plural society as well as reinforced a sense of inter-ethnic division (Haque 2003, p.244), and thus prevented any kind of unity and solidarity among the major ethnic groups (Stockwell 1982; Hirschman 1986; Sarji 1989). Under this policy, the Chinese were situated in the urban areas to work in the commercial and mining sectors, while the Indians laboured in the plantation sector, particularly on the rubber estates. Meanwhile, the Malays, who were the native people of Malaya, were primarily farmers and fishermen and lived in the countryside and rural areas (Mariappan 2002). Since these various ethnic groups generally lived in their own neighbourhoods, they commonly practised their own religion, spoke their own language, ran their own schools, and, later, established their own political organisations. For these reasons, the British policy has been alleged to be the strong

reason that diminished the unity of the ethnicities and races, emphasised the differences between the main ethnicities, and facilitated the social and economic imbalance in Malaya (Haque 2003). As Hirschman (1986, p.331) observes: "almost every writer who addresses the 'race problem' or the 'plural society' of Peninsular Malaysia suggests the roots of contemporary ethnic divisions and antagonisms were formed during the colonial era". Hence, the realisation of the differences in ethnicity that resulted from the policy has been one of the impediments to the Malaysian people declaring their identity based on nationality rather than ethnicity, and thus Malaysia remains a "deeply divided society" with "intensive socioracial cleavages" (Haque 2003, p.242).

The British colonial rule eventually ended when Malaya gained independence in 1957 and became known as the Federated States of Malaya. In 1963, Singapore, Sabah, and Sarawak achieved their independence from the British by joining the Federation States of Malaya, resulting in a larger geopolitical entity that has since been named Malaysia. Nevertheless, in 1965, Singapore was expelled from Malaysia due to the differences in ethnic policies. The Singapore leader, Lee Kuan Yew, expressed disagreement over the policies of preferential treatment for Malays and he advocated meritocracies instead (Singh 2001; Munusamy 2012). However, the fair and equal policy was not favoured by Malay leaders in Malaysia, since it opposed their view of the special rights of the indigenous people. It was for this reason that Singapore separated from Malaysia.

Moreover, it is interesting to mention that ethnicity largely influences the origin, substance, and legalisation of the major political parties in Malaysia (Haque 2003, p.246). For example, the Malays have their political party, United Malays National Organisation (UMNO), while the Chinese have their political party, Malayan Chinese Association (MCA), and the Indians formed their own political unit, namely, Malaysian Indian Congress (MIC). During the 60s, political parties, which were mainly ethnic-based, also had contradictory views and actions in their political modus operandi. During this time, UMNO was accused by Parti Islam SeMalaysia (PAS) of having a relaxed attitude to MCA's requests while MCA was accused of lenient acceptance of UMNO requests by the Democratic Action Party (DAP) (Munusamy 2012). While UMNO was trying to preserve the rights of Malays, the DAP objected to this by refusing the idea of having Malay as a main national language. The Malays'

burgeoning and long-standing frustration with the economic imbalances and the Chinese political resentment paved the way for ethnic tensions (Munusamy 2012).

Following a series of ethnic and political incidents, an ethnic riot occurred on 13 May 1969, an incident which permanently scarred the country. In this tragedy, hundreds were murdered or injured, and infrastructures and houses were destructed. The riot resulted in a state of national emergency and the suspension of parliament until 1971. Malaysian scholars have described the tragedy as having "put an end to the true consociation arrangement practiced from Independence in 1957" (Tan 2001, p.954). In the aftermath of the bloody incident, parliament passed a constitutional amendment that legally prohibited any public or media discussion of all sensitive issues involving ethnic constitutional rights. The bloody 13 May racial riot has since been an important lesson for the multiracial society in the nation to realise the importance of remaining united to maintain peace and live in harmony.

Furthermore, following the riot, policies such as the New Economic Policy, the National Culture Policy, and the Sedition Act were promulgated to mitigate the polarising issues. The NEP, for instance, was conceived with two aims in mind – to eradicate poverty and to eliminate ethnic inequalities (Gomez 2002; Mohamad-Yusof et al. 2018). Such policies sent a message to the communities that the Malay hegemony would not be removed easily (Mariappan 2002; Daniels 2005). In the new policy, a more drastic approach of promoting *Bumiputera*/Malay interests was initiated, such as facilitating easier access to government scholarships, public sector jobs, government contracts, and introducing a quota system for entry to public universities (Brown 2007; Cheong et al. 2009). Due to this ethnicity-laden landscape of the state in Malaysia, particularly in terms of its role in facilitating preferential treatments and policies in favour of the ethnic majority, it has been categorised as an "ethnocentric state" (Haque 2003, p.240).

2.5.3 Culture and ethnic differences in Malaysia

"…in our country, a Malay remains as a Malay, a Chinese remains as a Chinese, an Indian remains as an Indian, and every group has its own prejudices and sensitive aspects in which if extremely exploited will unleash its destructive effects"

(Former Deputy Prime Minister, Tan Sri Musa Hitam in Gale (1982))

Attributed to its diverse racial and ethnic composition as well as the occurrence of prior racial tensions, Malaysia has been often elucidated as "a minefield of cultural sensitivities" (Abdullah 2005, p.1). Yet, Malaysians today live harmoniously and peacefully together regardless of different ethnic and cultural backgrounds. Nevertheless, despite living together harmoniously as one nation, the majority ethnic groups in Malaysia (i.e., Malays, Chinese, and Indians) have significantly distinct cultural and religious heritages (Abdullah 1992; McLaren and Rashid 2002; Rashid and Ho 2003). They continue to maintain their separate identities while actively preserving their respective and distinct cultures, which influence their language, customs, dress codes, and behaviour patterns (Schermerhorn 1994; Rashid and Ho 2003). As articulated by Benhabib (2002, p.4), the "reductionist sociology of culture" emphasises the belief that each culture is naturally and irreducibly unique to an ethnic or racial group, which can be observed in each ethnic group in Malaysia (Lim 2008). Moreover, the obligation to preserve one's culture is indeed deeply ingrained yet unevenly heeded across Malaysia's multicultural communities (Lim 2008), and prevalent regardless of whether the community is Malays, Chinese, Indians, or other indigenous groups. As observed by Lim (2008), these individuals not only need to remember and preserve their own culture but at the same time implicitly embrace it as a unique way of life.

Social identity theory emphasises the notion of a person's knowledge and sense of belonging based on the certain social group they are in, along with considerable emotional and valuational significance of that group membership (Tajfel et al. 1979; Tajfel and Turner 1986). This theory relevantly applies to Malaysia's diverse ethnicity context, which propagates the inter- and intra-ethnic group relations. Verkuyten and Khan (2012) used a survey to access intergroup attitudes among the Malays, Chinese, and Indians in Malaysia, and, unsurprisingly, they found that the Malays hold a stronger national and ethnic identification and in-group bias in comparison to the Chinese and Indians. The preferential policies, special treatments, and political advantages given to Malays in Malaysia are the plausible factors that contribute to a higher national and ethnic identification among the Malays (Verkuyten and Khan 2012). In line with the results of prior studies in cross-national research (Elkins and Sides 2007; Staerklé et al. 2010), the study also finds that the ethnic minorities have lower national identification than dominant group members, similar to almost all

multiethnic nations. This validates the prevalence of substantial ethnic division and fault-lines among the Malays, Indians, and Chinese in Malaysia and becomes one of the conceivable barriers to the process of nation-building in Malaysia (Noor 2007). As Crouch (2001, p.227) observes: "there is a little progress toward ethnic assimilation. Malays remain Malays, and non-Malays remain non-Malays, with their own distinct senses of identity and their own political parties to defend their interest".

Although Malays, Indians, and Chinese live harmoniously in a nation while actively following their own traditions and preserving their own cultures and identities, their value systems appear to show some divergences. The substantial differences between the Malays, Chinese, and Indians have been reported by numerous Malaysian scholars (Abdullah 1992; Rashid et al. 1997; Rashid and Ho 2003; Abdullah 2005) and are summarised in **tables 2.6** and **2.7** below.

For instance, the Malay value system is encapsulated in the *budi complex*[7] (Dahlan 1991; Storz 1999), the Chinese value system is embodied by Confucianism (Storz 1999), whereas the Indians believe in Karma, which influences their actions to be more cautious and considers they have no control over their life (Rashid and Ho 2003). The divergence of their values and actions is also reflected in their differences in religions. By the Malaysian constitution, the Malays are Muslim and, as Muslims, they believe that one's destiny lies ultimately with Allah (Maniam 1986; Storz 1999). The majority of Chinese are Buddhist-Taoist and a small group embraces the Christian faith or respect for superstition (Wu 1980); whereas the Indians are predominantly Hindus, whose belief in the concept of rebirth influences their way of life. Differences between the three ethnic groups are also reflected in their behaviour, obedience to authority, facial traits, and relationship orientations (Rashid et al. 1997; Abdullah 2005).

Thus, since the cultures embedded with these three major ethnic groups are exclusively distinctive, it could be difficult to capture the prevailing societal values for the Malaysian nation as a whole. Therefore, the assumption of cultural homogeneity embedded in several influential cross-national values studies (Schwartz 1999; Hofstede 2001) may not be applicable to understand the cultural context in a multicultural society such as Malaysia. Although prior research has revealed the

[7] As mentioned by Dahlan (1991, pp. 46-47), *budi* "is composed of virtuous qualities such as generosity, respect, sincerety [sic], righteousness, discretion, feelings of shame at the collective level and a feeling of shame at the individual level".

divergence in cultural values between the Malays, Chinese, and Indians, there have been few investigations into cultural variations between these ethnic groups in business and workplace settings, and the results are equivocal. Using Hofstede's instrument, Lim (2001) finds that there are no cultural differences between Malay and Chinese senior executives. Similarly, using the Schwarz Value Survey to measure culture, Fontaine and Richardson (2005) confirm that the three ethnic groups show no significant divergence in the values of Conformity and Tradition and that only five of the 57 value items show substantial differences across the three groups in the workplace settings.

However, these results are overtly opposed to the prevalence of distinct ethnic heritages and cultural practices in Malaysia, particularly to the findings documented in the studies by Asma Abdullah and other Malaysian scholars (e.g., Rashid et al. 1997; Abdullah 2005). Utilising data obtained from a series of conferences, workshops, and seminars conducted in 1990 by the Malaysian Institute of Management, Asma Abdullah and her associates managed to compile a list of ethnic values incorporating the three major ethnicities in Malaysia. Until today, the list (refer to **Table 2.6)** has been widely referred to by numerous Malaysian scholars, particularly in examining the cultural differences among the Malaysian workforce.

In a more recent study, Zawawi (2008) updates the previous studies by exploring the similarities and differences of cultural values among the Malay, Chinese, and Indians. Meanwhile, Ramasamy et al. (2007) reveal that firms with Malay chief executives exhibit higher corporate social performance levels than companies with Chinese executives. The findings contradict some prior research examining the work-related values of Malays and Chinese that demonstrated there were no substantial variations between the Malays and Chinese, as both ethnic groups may have modernised their values under a shared wider social-cultural atmosphere (Abdullah 2005). Similarly, in the latest study, using the Schwartz Value Survey, Terpstra-Tong et al. (2014) reveal that Malay managers and professionals are more conservative and less self-transcendent than Chinese or Indian managers. Meanwhile, Ho (2010) explores how cultural values influence the ethnic group's ethical perception and finds that deviations in ethnical perception can occur when one culture assigns moral significance to something that another culture does not. Taken together, these studies contend that the

cultural values of each group are very deeply rooted and each group tends to carry some of its own cultural values even into the workplace and business settings.

Despite the above cultural values divergence between the Malays, Chinese, and Indians, the advice about staying true and remaining faithful to their own ethnicity and heritages has been routinely repeated and echoed over time in political gatherings and through mass media, thus, resulting in more separation of the diverse ethnic communities in Malaysia. Within all the ethnic groups, it is clear that the dominant group, the Malays, encounter the most vigilant conditioning and social monitoring to ensure that they never inadvertently neglect their race or the culture and religion that define it (Mariappan 2002). Due to the prior historical humiliation that they have suffered at the hands of other races in the past, the Malays are encouraged to preserve and embrace their race as well as to recognise their special rights as natives of Malaysia (Lim 2008).

As a consequence, this form of racial fuelling, recurring and echoing from time to time with various degrees of chauvinism, has promoted a more inward-looking, unreceptive, and defensive Malay community, even as it becomes growingly modernised (Lim 2008). The stoking of racial tensions has also become a conduit to emphasise the otherness of the non-Malays and to exacerbate their insecurity as minority groups situated within the hegemonic Malay circumstances (Lim 2008). Therefore, in the Malaysian context, the Malays will always identify themselves as Malays, the Chinese as Chinese, and the Indians as Indians, not just on the official forms, but stamped in their true selves, which subtly means that the ‘races’ and ‘ethnicities’ will remain protected, locked into their respective immutable heritages (Lim 2008).

Table 2. 6: Cultural profiles

This table exhibits some of the cultural values of the Malay, Chinese, and Indians in Malaysia based on the cultural profiles created by Abdullah (1992), McLaren and Rashid (2002), Rashid and Ho (2003) and Ho (2010).

Malay values	**Chinese values**	**Indian values**
Respect for elders	Hard work/diligence	Fear of God
Spirituality/faith in God	Success	Sense of belonging
Humility	Pragmatism	Brotherhood
Face/Self-respect	Perseverance	Family
Tack/indirectness	Wealth/Prosperity/Money	Hard work
Sensitivity to feelings	Face	Filial piety
Politeness	Harmony	Karma
Relationship oriented	Family oriented	Champion of causes
Apologetic	Risk-taking/gambling	Loyalty
Harmony	Position	Face
Loyalty	Filial piety	Harmony
Formalities	Entrepreneurship	Modesty
Accommodating		
Trustworthiness/Sincerity		
Teamwork		
Compliance		
Hierarchy/Obedience		
Non-confrontational		
Fairness		

Source: Abdullah (1992), McLaren and Rashid (2002), Rashid and Ho (2003) and Ho (2010)

Table 2. 7: Hofstede's social values applied to Malaysian ethnic groups

This table shows the Hofstede societal values of the three major ethnic groups in Malaysia: Malay, Chinese, and Indian.

Hofstede (Social value)	**Ethnic group**
Malay	**Malay**
Power distance	High
Masculine	Low
Avoiding uncertainty	High
Individualism	Low
Chinese	**Chinese**
Power distance	High
Masculine	Low
Avoiding uncertainty	Low
Individualism	High
Indian	**Indian**
Power distance	High
Masculine	Mid
Avoiding uncertainty	High
Individualism	High

Source: Haniffa and Cooke (2002)

2.5.4 The New Economic Policy and ethnic board representation in Malaysia

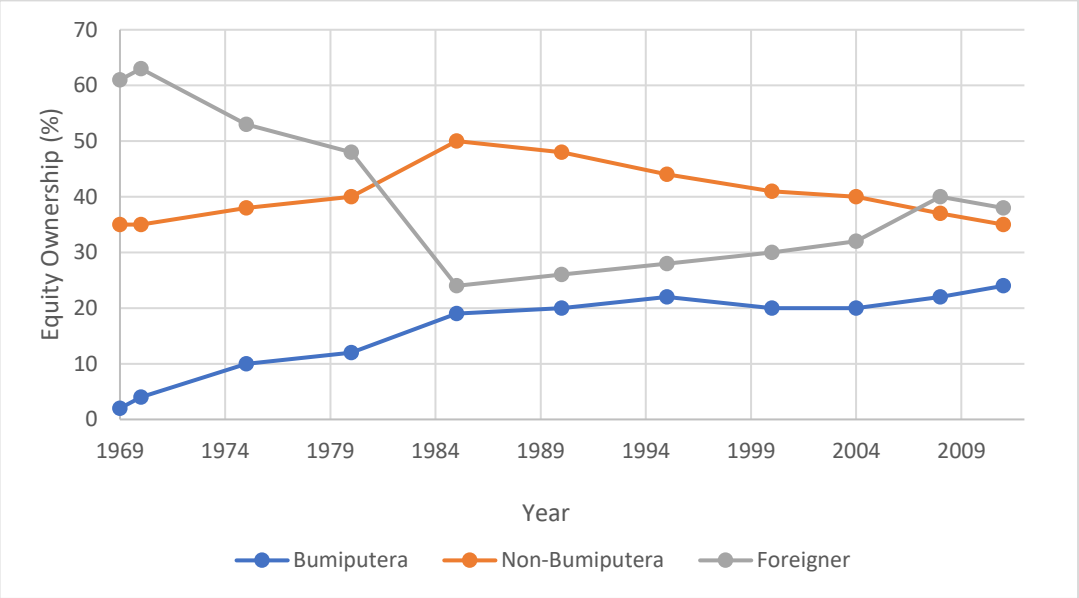
One of the most staggering courses of action by the post-colonial government to augment ethnic consciousness in Malaysia was through the introduction of the New Economic Policy (NEP) in 1970. Despite its title, the policy was introduced in 1970 in the aftermath of the tragic 13 May 1969 race riots which followed a few days after the 10 May 1969 general election. Although the reasons for the watershed events of the riot are still fairly ambiguous, many scholars and studies ascribed the riot as a result of economic disparities that occurred between the various ethnic groups, in particular between the Malays and the Chinese (Sundaram 1989; Jomo 1990; Doraisami 2012). Therefore, NEP was given twin objectives, which are to restructure the economy in order to eradicate poverty and to accomplish inter-ethnic parity between the ethnicities, in exchange for healthier ethnic integration, national unity, and social stability (Gomez 2002; Mohamad-Yusof et al. 2018). While Malaysia has three major distinctive ethnic groups, the Malays and the Chinese were the most prevalent ethnic groups in influencing and controlling the economic and political environment in Malaysia (Gomez 2002; Yatim et al. 2006). While the Malays influenced the country's politics and public services, the Chinese were mainly in control of business and the economy (Sundaram 1989). It was observable then that the Chinese capitalists gained economic prosperity but the Malays had restricted prospects to strive in the economic sphere, leading to resentment in the dominant ethnic group (Mariappan 2002; Yong 2004).

As a consequence of the government policy, major changes in Malaysia's corporate governance and economic landscape occurred in favour of accomplishing the interests of Malays and the indigenous ethnic groups, namely, *Bumiputera*. One of the changes encompassed the increase of the participation of *Bumiputera* in the corporate sector, joining their Chinese counterparts in shaping the business and economic environments in Malaysia. In pursuit of *Bumiputera* interests, the NEP sought to advance *Bumiputera* participation in the economy by ensuring the *Bumiputera* equity ownership to be at least 30% and encourage *Bumiputera* representation on corporate boards (Gomez 2002). With the help of the government's initiatives and economic expansion, the *Bumiputera* equity ownership increased gradually during 1970-1985 as did the non-*Bumiputera* equity, while the foreign ownership continued to decline (Mohamad-Yusof 2018). The privatisation policy during the mid-1980s also crucially

influenced equity ownership as *Bumiputera* ownership increased due to the blossoming of government-linked companies, whose board members were predominantly Malays (Jomo 1990; Gomez 2002). During the 1990s, there was an increase of *Bumiputera* ownership as the *Bumiputera* companies "started taking over Chinese business and there was a growing trend of *Bumiputera*-Chinese business partnership" (Cheong 1993, p.363; Mohamad-Yusof 2018).

Figure 2.3 exhibits the equity ownership in Malaysian companies from 1969 to 2011. As shown in **Figure 2.3**, the *Bumiputera* equity ownership gradually increased while the foreign ownership significantly decreased after the implementation of the NEP. Nevertheless, immediately after the Asian Economic Crisis in 1997/8, equity ownership of both the *Bumiputera* and non-*Bumiputera* declined. Nevertheless, in 2011, the *Bumiputera* equity had the highest level documented since the NEP had been implemented (Jalil 2015; Mohamad-Yusof 2018).

Figure 2. 3: Equity ownership in Malaysian companies from 1969 to 2011

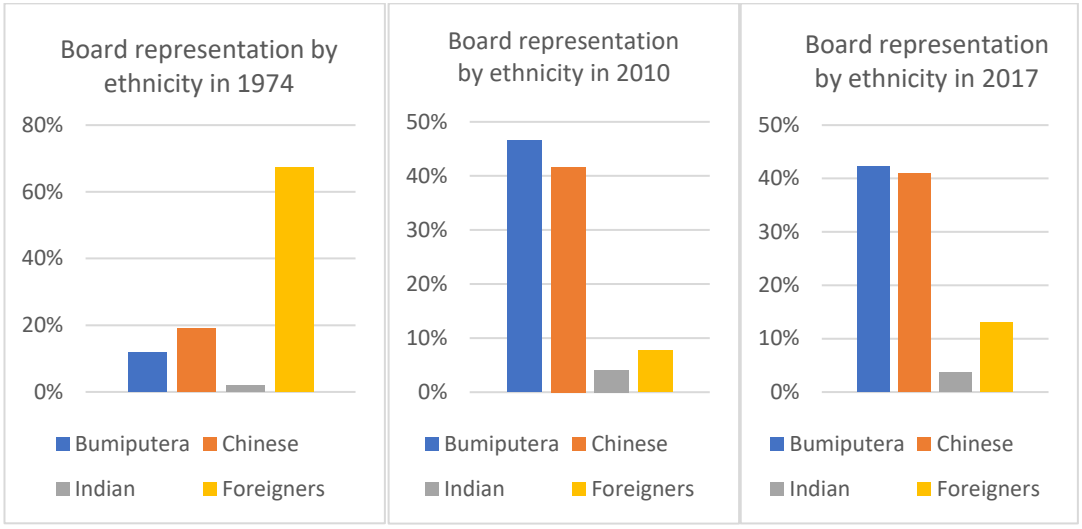


Source : Data extracted from Second Malaysia Plan, 1971–1975 (EPU 1971, p. 40); Third Malaysian Plan, 1976–1980 (EPU 1976, p. 184); Fourth Malaysian Plan, 1981–1985 (EPU 1981, p. 61); Sixth Malaysian Plan, 1990–1995 (EPU 1990, p. 13); Seventh Malaysian Plan, 1996–2000 (EPU 1996, p. 86); Ninth Malaysian Plan, 2006–2010 (EPU 2006, pp. 356–357); Tenth Malaysian Plan, 2011–2015 (EPU 2011, p. 148); Prime Minister's speech on the Eleventh Malaysian Plan, 2016–2020 (EPU 2015, p. 7); and Mohamad-Yusuf et al. (2018).

Meanwhile, *Bumiputera's* representation on corporate boards of directors appeared to increase with the promulgation of the NEP even though foreign directors dominated the boards (Mohamad-Yusof 2018). During the first years of the policy, Malay directors were not engaged exclusively in managing the business but merely acted as 'functional directors' who embodied extra-economic roles for the corporation and often emblematically represented the *Bumiputera* (Lim 1981; Mohamad-Yusof 2018). Their presence was primarily for political business agenda for "access to state rents, expediting bureaucratic decisions of business ventures, or bypassing state regulation of greater *Bumiputera* participation among the owners of listed companies" (Gomez 2002, p.90). As a result, many prominent Malay figureheads, elites, and civil servants who were affiliated with a dominant political party such as UMNO were appointed to hold non-executive director roles as their presence was essential to gain those benefits (Gomez 2002; Mohamad-Yusof 2018). The growing *Bumiputera* interests in public listed companies during the 1990s also resulted in an upsurge in the number of Malay directors and they began to dominate the boards of directors (Mohamad-Yusof 2018).

Figure 2.4 indicates that *Bumiputera* still have a substantial and perennial presence on corporate boards, as shown by evidenced from the top 100 companies listed on Bursa Malaysia. Thus, it is considered that ethnicity is embroiled in corporate ownership structures and board representation as a result of the *Bumiputera* influence as well as the formation of the NEP. As a consequence, the majority of boards across the corporate sector in Malaysia today consist of representation from diverse ethnic groups and more than one ethnic group (Gul et al. 2016), making Malaysia a unique setting to examine our research questions, particularly on the effect of ethnic (cultural) similarity between CEO and board of directors on board monitoring and firm performance.

Figure 2. 4: Board representation in Malaysia by ethnicity in 1974, 2010 and 2017



Source: Data extracted from the annual report of 100 companies on Bursa Malaysia in 2010 and 2017 and Mohamad-Yusuf et al. (2018)

2.5.5 Empirical studies on ethnic board diversity in Malaysia

Due to the pervasiveness of ethnic board representation in Malaysia, recent studies on Malaysian corporate board settings have shown an increasing interest in board ethnic diversity. As indicated by Ahmad-Zaluki (2012), the Malaysian listed firms are ethnically diversified and their board members consist of various ethnic groups in Malaysia influenced by the multicultural community. Furthermore, Yatim et al. (2006) reveal that the ethnicity factor influences the condition of corporate governance in Malaysian firms. Consequently, numerous Malaysian scholars have taken advantage of the unique multicultural society in examining the effects of board ethnic diversity on organisational outcomes. However, although the scholars have shed valuable insights into the effects of ethnic board diversity on governance outcomes, the findings are equivocal. Marimuthu and Kolandaisamy (2009) is one of the earliest studies to examine the effect of ethnic diversity on firm profitability. Using the top 100 Malaysian firms over the period 2000 to 2006, the study finds a positive association between the ethnic diversity of boards and firm performance, as measured by return on assets and return on equity, implying the positive effect of diversity on firm performance. This view is supported by Shukeri et al. (2012), who write that larger ethnic diversity facilitates information sharing and enables ultimate decision-making based on diverse views, and thereby improves a firm's operating performance. Using

Tobin's Q as a measure of firm financial performance, Cheong and Sinnakannu (2014) also find a positive relationship between ethnic diversity and firm financial performance. Unlike both Marimuthu and Kolandaisamy (2008) and Shukeri et al. (2012), the study, however, reports no significant relationship between ethnic diversity and a firm's book measure of financial performance. Moreover, the study further reveals that firms with higher profitability attract greater ethnic diversity.

While the aforementioned studies demonstrate the positive effect of board ethnic diversity on firm performance, Gul et al. (2016) find that the effect is inconsistent. Using a more recent sample of Malaysian firms than those in prior studies, the findings of Gul et al. (2016) are contrary to the studies mentioned above as the relationship between board ethnic diversity and firm performance appears to have a non-linear outcome. At the lower levels of ethnic diversity, the firm performance is observed to be improved; however, at the progressively higher levels of ethnic diversity, the association between board ethnic diversity and firm members gradually lessens and becomes negative.

Another study that has examined the effect of ethnic board diversity in the Malaysian setting is that of Abdullah et al. (2016). Specifically, this study focuses on the effect of ethnic board diversity on the relationship between the participation of women on boards and accounting performance as measured by return on assets. As ethnicity forms people's perceptions of the world, it is also predicted to influence the nomination process of women and the essence of their board participation (Abdullah et al. 2016). Using a dataset of 841 firms listed on the Main Board on Bursa Malaysia, the study, however, finds no significant effect of the ethnically diverse board on the association between the presence of women on boards and accounting performance. Meanwhile, in a more comprehensive and recent board diversity study, Hassan and Marimuthu (2018) examine the effects of demographic diversity dimension including ethnic diversity at the top-level management on firm financial performance. Similar to prior studies (Marimuthu and Kolandaisamy 2008; Shukeri et al. 2012), the study shows that ethnically diverse boards appear to have a significant and positive impact on firm financial performance.

Apart from the above studies that have focused on the effects of ethnic board diversity on firm financial performance, others have directly examined the impact of ethnic

board diversity on the quality of information disclosures. One such study, conducted by Katmon et al. (2019), has examined 200 listed Malaysian firms to find out the impact of broader dimensions of board diversity including ethnicity on the quality of corporate social responsibility (CSR) disclosure. Nevertheless, the authors find that an ethnically diverse board has no significant relation with the quality of CSR. Another important study that has examined the association between ethnically diverse board size and the quality of information is that of Tee and Rassiah (2020). Using reported earnings as the main indicator of information quality, the study argues that ethnically heterogeneous boards reduce the social cohesiveness among directors from the same ethnic group, enhance the quality of board monitoring, and thereby improve earnings quality. The study finds that boards with higher ethnic diversity are significantly associated with higher earnings quality. Further, the study also ascertained that ethnically diverse boards attract more institutional investors.

Collectively, the above studies outline a critical role of diverse ethnicity within Malaysian corporate boards on various organisational outcomes. Although previous research findings have been inconsistent and contradictory, ethnicity has been one of the fundamental elements that characterise Malaysian corporate boards due to the nation's multiculturalism feature and "environment where there are close links between ethnicity, politics, and business" (Gul et al. 2016, p.116). While the above studies focus on how ethnic diversity among board members affects firm performance and various organisational outcomes, little is known about the effect of ethnic/cultural similarity between top management and board of directors. Examining the behaviour and interaction outcomes of the two important parties (i.e., management and board) while investigating how ethnicity or cultural factor affects their fiduciary roles is important, as such interactions may affect the effectiveness of corporate governance and shareholder wealth (Adams and Ferreira 2007; Hwang and Kim 2009). Thus, our study fills the void in the literature by providing evidence of the effect of CEO-board cultural similarity on the perspectives of firm value and board monitoring effectiveness as well as managerial entrenchment.

2.5.6 Overview of corporate governance in Malaysia

Since the aftermath of the Asian financial crisis in 1997/98, corporate governance has increasingly been acknowledged as a crucial issue due to the prior corporate failures

and severe shortcomings in the existing governance system (Calomiris 1998). The Malaysian government and regulators have realised the weakness of Malaysian corporate governance and formed several initiatives to enhance the country's corporate governance system (Alnasser 2012). The Malaysian government's earliest initiative in ensuring corporate governance practices were in place was in March 1998, when the government established the High-Level Finance Committees on Corporate Governance and the Malaysian Institute of Corporate Governance (Securities Commission Malaysia 2018). The collaborative initiative between the government and the private sector aimed to set up a framework for corporate governance and establish industry best practice. In 1999, the committee produced its report documenting three key elements, which are: revising relevant laws, announcing mandatory training for directors, and augmenting the Malaysian Code on Corporate Governance (MCCG 2000) (Securities Commission Malaysia 2018).

In 2000, the Minority Shareholder Watchdog Group (MSWG) was established to mainly promote good corporate governance practices in the capital market as well as to protect the interests of minority shareholders (Mohamad-Yusof 2018). Modelled on the UK corporate governance conduct, the first Malaysian Code on Corporate Governance was developed and introduced in 2000. It highlights the guidelines on board structure and composition, measures for recruitment and remuneration of directors, and the role of board committees as well as internal controls. In addition, the code also enhances the board independence regulations by advocating that boards should include non-executive directors including independent non-executive directors (Securities Commission Malaysia 2018).

In 2007, the code was reviewed and revised to reinforce the functions of the board of directors, audit committee, and internal audit, and ensure their roles were effective to govern the firms (Mohamad-Yusof 2018). Moreover, the revised code highlights the composition and structure of the audit committee, the frequency of board meetings, and the imperative of continuous training. Internal audit roles are now compulsory in all public listed firms and the reporting line for internal auditors has been organised (Mohamad-Yusof 2018). In 2010, the Auditor Oversight Board (AOB) was established to facilitate an effective and vigorous audit oversight framework in Malaysia. Moreover, the Capital Market and Services Act (2007) was revised in the same year in order to sanction the Securities Commission to take action against

directors who bring unlawful damage to listed companies (Securities Commission Malaysia 2018).

In 2011, the Corporate Governance Blueprint 2011 was launched to advocate better internationalisation of good governance principles and outline strategic initiatives for stronger market discipline. It also mandated the establishment of a nominating committee and reviewed the expansion of integrated reporting. In 2012, the MCCG was further revised to reinforce board structure and composition. It also highlights the best practices for strengthened board independence, the integrity of financial reporting, directors' remuneration, and the relationship between the company and shareholders. In 2017, the new code (MCCG 2017) was released to replace the 2012 code with the purpose of advancing the standards of corporate governance of firms in Malaysia. It proposed the CARE method, which is an abbreviation of the term 'Comprehend, Apply and Report', which encourages firms to 'apply or explain an alternative' method and to make a transit from the existing 'comply or explain' method (Mohamad-Yusof 2018). It also advocates principles for strengthened board independence, board diversity, and transparency in directors' remuneration. **Table 2.8** summarises this development.

Table 2. 8: Corporate governance developments in Malaysia

Year	Key corporate governance developments in Malaysia
1998	High-level Finance Committee on Corporate Governance established Malaysian Institute of Corporate Governance established Code of Ethics for Directors by Companies Commission Malaysia introduced
1999	High-Level Finance Committee Report on Corporate Governance
2000	Malaysian Code on Corporate Governance (MCCG 2000) introduced Minority Shareholder Watchdog Group (MSWG) established
2001	Capital Market Masterplan (CMP) established Revamp of Corporate Governance section in Bursa Malaysia Listing Requirements
2004	Provisions regarding whistleblowing and redress mechanism for breaches of securities laws were amended in the securities laws
2007	Revision to the Malaysian Code on Corporate Governance (MCCG 2007) Companies Act (Amendment) 2007 Capital Markets and Services Act 2007 (CMSA)
2010	Bursa Malaysia's Corporate Governance Guide 11th Edition Amendments to CMSA empowering SC to prosecute CG transgressions Audit Oversight Board established
2011	Capital Market Masterplan 2 – Growth with Governance Corporate Governance Blueprint 2011 launched ASEAN CG Scorecard
2012	Listing Requirements (LR) amendments on Related Party Transactions, CG, and internal control disclosures Malaysian Code on Corporate Governance 2012 (MCCG 2012) released
2017	New Malaysian Code on Corporate Governance (MCGG 2017) released Institute of Corporate Directors Malaysia established Bursa Malaysia's Corporate Governance Guide 2017 LR amendments on new CG reporting approach and format

Source: Securities Commission Malaysia (2018) and Mohamad-Yusof et al. (2018)

2.6 Chapter summary

This second chapter of the thesis has reviewed the related literature and empirical studies that are relevant to our topic and crucial in catalysing the theoretical foundations for this thesis. Due to the interdisciplinary nature of this thesis, this chapter has drawn from various disciplines including corporate governance, sociology, finance, and culture. It first discussed the influential roles of the board of directors based on the lens of two influential corporate governance theories: agency theory and resource dependence theory. The novel theory of the board of directors, which is the behavioural theory, was also discussed in this chapter. Together, these theories provide insights into the functions of the board of directors, as a key internal corporate governance mechanism. Further, this chapter discussed the ramifications of CEO-director ties by reviewing the extant literature on CEO-director ties. The related theories of cultural similarity, homophily theory and social identity theory, were also discussed together with the existing empirical studies that were developed based on these theories. We also presented the implications of cultural ties together with the related literature. Next, the influence of culture on corporate governance and finance as well as the bottlenecks of the existing cultural dataset and measurement were also highlighted in the chapter. Reflecting on the prior studies on the role of culture in corporate governance as well as the fragility of the current cultural measurements, this chapter also discussed the measurement of CEO-board cultural similarity used in this thesis. Finally, this chapter also provided the institutional background of the topic as well as the related Malaysian studies.

After reviewing all the theories and related studies, we aim to address the following gaps in the literature. While numerous studies have investigated the impact of social ties between CEO and directors that have been achieved through the achieved status or experiences such as through employment, membership, alma mater on various corporate outcomes, there has been relatively little work concerning the effect of the CEO-board cultural similarity on governance outcomes. Since ethnicity or culture is amongst the most important salient characteristics owned by individuals, this study fills the gap in the literature by investigating the role of CEO-board cultural similarity in the value-creation process and the effectiveness of board monitoring. Furthermore, previous studies have provided shreds of evidence on the significant impact of cultural similarity on various economic exchanges and corporate decisions. Nevertheless, there

is little direct evidence in corporate governance of the ways through which culture affects interactions between the key corporate governance actors, especially in the dyad of CEO and board of directors. Based on the homophily theory and social identity theory, we postulate that cultural similarity between CEO and board of directors helps form a social tie between these two parties, and therefore our study aims to highlight the implications of such ties on firm value and governance outcomes

Moreover, numerous studies have extensively investigated the influence of culture on finance and corporate governance from various perspectives. However, the impact of culture on corporate boards is somewhat neglected. Therefore, the present study seeks to fill the gap by investigating whether culture plays a significant role in the relationship between CEO and board and how having a CEO and directors from a similar cultural background affects firm performance and board monitoring. In fact, the cultural differences or similarities between this dyad (CEO-board) have not been considered in the corporate finance and corporate governance literature. Thus, we introduce a novel concept within these fields by measuring CEO-board cultural similarity to examine the impact of cultural factors in corporate boards on firm performance and board effectiveness.

Furthermore, although previous research focused on how ethnic diversity among board members affects firm performance and various organisational outcomes, the literature remains silent on the effect of ethnic/cultural similarity between top management and board of directors. Investigating the behaviour and interaction outcomes of the two important parties (i.e., management and board) while investigating how ethnicity or cultural factor affects their fiduciary roles is important, as such cultural ties may affect the effectiveness of corporate governance and shareholder wealth (Adams and Ferreira 2007). Thus, our study fills the void in the literature by providing evidence of the effect of CEO-board cultural similarity on the perspectives of firm value, board monitoring effectiveness, and financial reporting quality as well as managerial entrenchment.

Chapter 3

CEO-Board Cultural Similarity and Firm Value

3.1 Introduction

In this chapter, we explore the relationship between CEO-board cultural similarity and firm value to empirically answer the following research questions*: does CEO-board cultural similarity influence firm value?* and *does CEO-board cultural similarity affect board independence and the effectiveness of the monitoring function of the board of directors?*

Given the wide-ranging evidence from the sociology literature (McPherson et al. 2001) that 'similarity breeds connection' among people and 'birds of feather flocks together', we hypothesise that similarity in cultural values may serve as an important conduit through which social connections and relationships are developed. We extend this line of inquiry to the context of corporate boards and offer new insights on how similarity in cultural backgrounds between managers and board directors affects boards' monitoring effectiveness and firm value. Specifically, we first empirically address the following questions: *does CEO-board cultural similarity influence firm value?* and *how?*

As suggested by prior literature, strong CEO-director ties can be either detrimental or beneficial. On the one hand, the strong ties between the CEO and the board facilitate the effective functioning of the board, which in turn enhances firm values. Drawing on resource dependence and homophily theories, we argue that the shared common cultural background between the two parties may provide an emotional bond and foster mutual trust between them (Westphal 1999; McPherson et al. 2001; Leszczensky and Pink 2019). In turn, such relations provide superior communication, collaborations, and information flows between the parties, all of which are necessary to ensure the effectiveness of the board's advisory role (Westphal 1999). The reduced

information asymmetries due to pre-existing connections between the board and the CEO may result in quicker, more efficient, and superior joint decision-making (Adams and Ferreira 2007). Hence, under this 'bonding' view, the shared values and beliefs due to similar cultural or ethnic backgrounds improve the effectiveness of the board's advisory role, which in turn enhances shareholder value.

On the other hand, the strong ties between CEO and board exert a negative influence on firm value. According to social theories, since similarity breeds empathy, acceptance, and friendships among individuals (McPherson et al. 2001), cultural similarity may be conducive to a close and empathetic relationship between the CEO and the board, thereby hindering the latter's exercising of due diligence in their monitoring tasks. Moreover, the intimacy derived from the shared cultural values between the two parties may subject the board's decisions and judgments to potential biases, resulting in agency costs. Hence, boards may be prone to making decisions that favour the CEO at the expense of shareholder value, leading to an erosion of firm value (Fracassi and Tate 2012; Fan et al. 2019). Overall, whether and how the cultural connectedness between CEOs and board members affects firm value is ultimately an empirical question.

Using a sample of 621 non-financial Malaysian firms over the period 2009-2016, we find that cultural similarity between CEOs and the board of directors (henceforth referred to as 'cultural similarity'), measured as the fraction of board of directors who have the same ethnicity as the CEO, is negatively and significantly related to firm value. In terms of economic significance, a one-standard-deviation increase in cultural similarity is associated with a 6.14% decline in firm value. Our results are robust to alternative model specifications, alternative variable definitions, and endogeneity tests.

We further empirically address the following question: *does CEO-board cultural similarity affect board independence and the effectiveness of the monitoring function of the board of directors?* Motivated by existing studies that incorporate the social ties into the definition of true independence (e.g., Hwang and Kim 2009), we further examine the differential association between board independence and firm value when we replace the formal measure of board independence (which does not consider CEO-board cultural ties) with our new measure of board independence. Under the new

measure, a director is identified as independent if he or she is an independent director and also culturally independent of the CEO. We find a positive relationship between our proposed measure and firm value. These results suggest that cultural ties are value-relevant and act as a medium of CEO-board relationship, which consequently may impair the effectiveness of board independence

Further analysis shows that firms with a greater degree of cultural similarity hold fewer board meetings, which is consistent with reduced effectiveness in board monitoring. As an additional test of the relevance of cultural similarity ties, we examine whether board independence moderates the relationship between cultural similarity and firm performance. We find that the negative effect of CEO-board cultural similarity on firm value is stronger among firms with highly independent boards. Thus, since independent boards are commonly associated with higher monitoring quality and lower agency costs (Fama and Jensen 1983; Eisenhardt 1989; Bhagat and Black 2001; Hermalin and Weisbach 2003; Hillman and Dalziel 2003), our results signify that cultural similarity impairs the effectiveness of board independence. Furthermore, our main results also hold significantly even after controlling for the political connection feature, as proxied by Malay CEOs and boards.

This study contributes to the growing stream of research on the effects of the CEO-director relationship on corporate outcomes. There appears to be a consensus in the literature that social reciprocity between CEO and other directors weakens the board's monitoring intensity and reduces firm value (e.g., Hwang and Kim 2009; Fracassi and Tate 2012; Lee et al. 2014; Goergen et al. 2015). We extend this literature by highlighting the adverse impact of common cultural values between the CEO and other board members on board monitoring and firm value. Combining several board theories (e.g., agency and resource dependence theory) as well as sociology theories (e.g., homophily and social identity theory), our study shows that CEO-board cultural similarity reduces firm value and monitoring effectiveness as well as board independence.

Furthermore, due to the influence of culture as an informal institution on economic outcomes, numerous studies have attempted to explain the role of various aspects of culture in business practice, corporate decision-making, and organisational outcomes. Specifically, prior research shows that culture affects corporate risk-taking (Li et al.

2013), corporate disclosure (Haniffa and Cooke 2002; Qu and Leung 2006), earnings management (Zhang et al. 2013), and corporate financing decisions (e.g., Shao et al. 2010; Zheng et al. 2012). We contribute to this line of research by highlighting the relevance of cultural similarity between CEO and board of directors to the board's monitoring effectiveness and governance quality.

The remainder of the chapter is organised as follows. The next section develops our main hypotheses. **Section 3.3** presents data and descriptive statistics. S**ection 3.4** reports the results and **Section 3.5** concludes the chapter with a summary and discussions.

3.2 Hypotheses development

The sociology literature identifies several grounds through which human beings can interact and build social connections with others. Based on the homophily theory that advocates 'similarity breeds connections' and 'birds of a feather flock together' (McPherson et al. 2001), we elucidate that similarity in cultural background and values could also catalyse and facilitate relationships among individuals. As a "glue that holds its members together through a common language, dressing, food, religion, beliefs, aspirations, and challenges" (Abdullah 1996, p. 3), culture play a significant role in forming an invisible bond that can tie individuals together and establish a basic social network among them. Due to the shared and common cultural values and attributes, research has also revealed that culturally similar individuals are more likely to be associates than are individuals who are culturally different (Byrne 1971; Kandel 1978; Leszczensky and Pink 2015, 2019), which is in line with the argument of McPherson et al.'s (2001) homophily theory.

The cultural similarity between individuals could also establish greater ties, communication, and trust among them. As argued by McPherson et al. (2001), individuals typically have better communication and mutual understanding when interacting with their values and beliefs counterparts (McPherson et al. 2001). Such similarities may facilitate a better flow of information and build trust between individuals and consequently lead to better cooperation and decision-making. Furthermore, as "socially situated and constituted agencies", corporate decision-makers such as boards can have "multiple social identities", and the agencies and such corporate environments are neither free from the social attribute (Westphal and Zajac

2013, p.624) nor culturally free (Guiso et al. 2006). Thus, we argue that, within the corporate board environment, the cultural similarity between CEO and directors could establish a bond between them which could enhance the board's advisory role, through their close kinship.

Drawing on resource dependence theory, prior studies assert that management-board social ties create social capital, which is defined as a firm's valuable asset and resource for the practice of its strategy and thus affects firm value (Pfeffer and Salancik 1978; Nahapiet and Goshal 1998; Hillman et al. 2009). In this perspective, boards of directors are considered as valuable providers of resources in their functioning role as advisors for managers, particularly on firm strategy and other corporate decision-making issues (Westphal 1999; Adams and Ferreira 2007) Prior studies also indicate that CEO-director ties facilitate greater board involvement and collaboration, leading to an increase in board effectiveness, which can contribute positively to firm value (Fracassi and Tate 2012; Fan et al. 2019). Consistent with prior studies, we posit that cultural similarity between CEO and directors is a conduit for valuable information flow, which can emphasise the board's advisory role, leading to efficient strategy and decision-making. Thus, drawing from the theory of boards of directors and sociology literature, we posit that CEO-board cultural similarity could enhance the board's advisory function, leading to an increase in firm value.

In contrast, cultural similarity can form a prominent basis of self-identity and social identity, which refers to in-group members extending preference and favour to each other over the out-group members in terms of behaviours, attitudes, preference, or perception (Turner et al. 1987; Hewstone et al. 2002). This could also lead to in-group favouritism and biases elicited by such similarity, as suggested by the social identity theory (Tajfel and Turner 1986). Thus, we postulate that this in-group favouritism and biases derived from the shared cultural background inhibit the directors' monitoring and overseeing effectiveness.

Drawing from agency theory, boards play an important role in resolving the 'agency problem' by controlling potentially misaligned managers/CEOs through monitoring and incentives (Fama and Jensen 1983). Nevertheless, a growing body of literature suggests that the shared characteristics and values between top management and the board of directors can be detrimental to effective decision-making and board

effectiveness. For example, Nguyen (2012) shows that social connections prevent boards from monitoring CEOs effectively. Other studies also find that other types of similarities – including those related to the country of origin, schools, club membership, age, and political orientations – weaken board independence and the monitoring role of outside directors (Hwang and Kim 2009; Lee et al. 2014; Goergen et al. 2015). This is because the social ties derived from such similarity would decrease the board's willingness to discipline the CEO, destroying the firm's value when the preferences of the CEO and the shareholders are not aligned. Consistent with these studies, the CEO-director's cultural similarity can also be a signal of weak corporate governance to the market, leading to destruction of firm value. Thus, based on the theoretical arguments, we infer that the cultural similarity between the CEO and other directors may exacerbate group biases as well as agency problems that could impair the board's monitoring effectiveness and ultimately destroy the firm's value.

Overall, these theoretical arguments infer that CEO-director's cultural similarity may, on one hand, improve the board's advisory role through greater communication, strategy, and decision-making, leading to an increase in firm value, while, conversely, it may weaken the monitoring role of the board, leading to an erosion in firm value.

Hypothesis 1a: *Cultural similarity between CEO and other board members has a positive and significant effect on firm value*.

Hypothesis 1b: *Cultural similarity between CEO and other directors has a negative and significant effect on firm value*.

3.3 Sample and variable measurements

3.3.1 Data and sample selections

Our sample includes all non-financial firms listed on the main market of Bursa Malaysia (previously known as Kuala Lumpur Stock Exchange) during the period 2009-2016. Finance-related service firms were excluded, as they are based on different regulations and operate under close supervision from the Central Bank. Meanwhile, the period 2009-2016 represents a period in which Malaysia's financial and economic

conditions were relatively stable after the 2007-2008 global financial crisis.[8] Our sample period also enables us to consider the effect of corporate governance reforms in 2012. The revised Malaysian Code on Corporate Governance (MCGG 2012) was released in 2012, aiming to strengthen the board structure and composition while reinforcing the role of the board of directors as key actors in providing a more meaningful and independent oversight function. After excluding observations with incomplete data, our final sample consists of 5,157 firm-year observations from 621 unique firms. Financial and accounting data were retrieved from S&P Capital IQ and DataStream, while non-financial information and corporate governance data were manually collected from annual reports, retrieved from the Bursa Malaysia website (www.bursamalaysia.com) and Bloomberg. The detailed sample selection process is shown in **Table 3.1.**

Table 3. 1: Sample selection process

This table reports the sample selection process and resulting firm-year observations. We begin with all listed firms on Capital IQ from 2009 to 2016. After deleting observations in financial and regulated industries as well as observations with incomplete financial and governance data, we have 4,392 from 2009 to 2016.

No		Number of observations
1	Total number of firm-year observations from 2009 to 2016	7,448
2	Observations in financial and regulated industries	(1,327)
3	Observations with incomplete data (financial or corporate governance)	(1,729)
	Final sample	4,392
	No of unique firms	621

3.3.2 Measuring firm value

Following others (e.g., Hwang and Kim 2009; Fracassi and Tate 2012; Lee et al. 2014; Goergen et al. 2015), we use Tobin's Q (*Tobin's Q*), computed as the book value of total assets minus the equity, all divided by the book value of assets, as a measure of firm value. Compared to accounting-based firm-performance measures, *Tobin's Q* is more forward-looking, captures the firm's current performance and the market

[8] The quality of data in the earlier period (i.e., the 1990s) is rather poor, making it difficult to produce reliable results. Furthermore, lack of corporate governance reforms and structures in earlier periods (Malaysia's Corporate Governance Code was first initiated in 2000) makes it difficult to draw inferences about the governance role of cultural similarity.

expectations about its prospects, and is less affected by accounting conventions or potential earnings manipulation (Lubatkin and Shrieves 1986; Gentry and Shen 2010). Meanwhile, accounting measures, such as ROA, are under greater control by managers, and, hence, they are more likely to reflect a CEO's effort to maximise profits (Chakravarthy 1986; Gentry and Shen 2010). To mitigate the effect of outliers, we winsorise *Tobin's Q* at the 1% level on each side of the distribution.

3.3.3 Measuring cultural similarity

The measurement of cultural similarity and the construction of our key variable of interest, the cultural similarity between CEO and other board directors (*Cultural Similarity*), were previously discussed in more detail in **Section 2.4.4.**

3.3.4 Control variables

Several firm characteristics that are important to firm value are controlled for in our analysis. *Firm Size*, measured as the natural logarithm of total assets, is considered an important determinant of governance and firm performance (Gabrielsson and Winlund 2000; Orlitzky 2001). *Firm Age*, as measured by the number of years since the firm's founding, has also been suggested as a relevant variable influencing a firm's growth and performance (Thornhill and Amit 2003; Ling et al. 2007). *Sales Growth* is the annual growth rate of a firm's total sales, which reflects its growth opportunities. *Leverage* is calculated as the firm's debt to assets ratio (total debts divided by total assets). A firm's audit quality (*Big4 Auditor*) is captured by a dummy variable that equals one if it is audited by Big 4 auditors, and zero otherwise. Finally, we also include *R&D*, which is computed as the annual R&D expenditures divided by total revenue, both measured at the end of fiscal year t-1, as one of the control variables (Belderbos et al. 2004).

We also include firm governance characteristics by incorporating board size, board independence, and board meetings variables. Several studies report a positive relationship between board size and firm performance (Pearce and Zahra 1992; Coles et al. 2008; Fauzi and Locke 2012). These studies argue that large boards have directors from diverse backgrounds, knowledge, and intellect, which can be used for effective decision-making and strategic planning in the organisation. However, prior literature documents a negative association between board size and firm performance (Jensen 1993; Yermack 1996; Hermalin and Weisbach 2003), arguing that board

members are less likely to function effectively and CEOs may find it difficult to participate when boards are too big. Hence, we include *Board Size*, measured by the number of directors on the board, in our study.

The presence of independent directors is essentially recommended in both national and international corporate governance codes since such directors could reduce agency problems by exercising proper oversight function over monitoring governance, internal control, and risk management. Although several studies document a positive association between the number of independent directors on the board and firm performance, others find board independence yields poor monitoring and hence poor performance (Bhagat and Black 2001; Hermalin and Weisbach 2003). Due to its potential effect on firm performance, we also include *Board Independence*, expressed as the percentage of independent directors on the board, as a control variable.

With respect to the board meetings, as one of the corporate governance mechanisms, two insights arise from the previous literature. The first is derived from the agency theory, which indicates that board meetings are beneficial in terms of effective management monitoring that can have important implications for firm value (Vafeas 1999; Adams and Ferreira 2007). The second insight, however, suggests that boards should be relatively inactive to avoid any potential issues that might arise due to the regular meetings (Jensen 1993). We include *Board Meeting*, measured by the number of annual board of directors meetings, as another control variable in our regressions. Detailed variable definitions can be found in **Table 3.2**.

Table 3. 2: Variable definitions and data sources

Variable	Definition	Sources
Dependent variables		
Tobin's Q	The book value of total assets minus the book value of equity plus the market value of equity, all divided by the book value of total assets; log-transformed	Capital IQ
ROA	Industry-adjusted ROA and calculated as operating income divided by the year-end book value of total assets; scaled and log-transformed	Capital IQ
Independent variables		
Cultural Similarity	The proportion of board directors that share similar cultural/ethnicity backgrounds with the CEO, i.e., the number of directors that share a similar ethnic background with the CEO/total number of directors	Bloomberg and annual report
Board characteristics		
Board Size	The number of directors on the board; log-transformed	Annual report
Board Meeting	The number of annual boards of director meetings; log-transformed	Annual report
Board Independence	The percentage of independent directors on the board	Annual report
Firm characteristics		
Firm Size	The natural logarithm of total assets	Capital IQ
Firm Age	The number of years since the firm's founding; log-transformed	Capital IQ and annual report
Firm Leverage	Total debt to assets (total debts divided by total asset; log-transformed	Capital IQ
Big 4 Auditors	An indicator variable with the value of one if audited by Big 4 auditors, and zero otherwise	Annual report
Sales Growth	The annual growth rate of the firm's total assets; scaled and log-transformed	Capital IQ
R&D	The annual R&D expenditures divided by total revenue, both measured at the end of fiscal year t-1. Missing R&D values are set to zero; scaled and log-transformed	Capital IQ
Market-to-Book Ratio	(market price of share) divided by (shareholders' equity divided by the number of ordinary shares outstanding)	Capital IQ

3.3.5 Descriptive statistics and correlation matrix

Table 3.3 presents the descriptive statistics of the variables used in our analysis. The average proportion of board members that share cultural similarity with the company CEO (*Cultural Similarity*) is 0.69, implying that the majority of the directors on the board share similar culture/ethnicity with their company's CEOs. Moving to the governance variables, the average *Board Size* is about 7 members, ranging from 3 to 22 members. The average *Board Independence* is 47%, ranging from 11% to 100%. The average frequency of *Board Meeting* in a year is 5 times and ranges from 0 to 27 times per year. For firm characteristic variables, the average size of firms is 2053.47 million MYR and the average firm age is 28.75 years. The average of *Tobin's Q* is 1.22. The large variation in the *ROA* indicates that Malaysian companies differ greatly in their profitability. These statistics differ slightly from those of Gul et al. (2016) and Bhatt and Bhatt (2017), presumably because our sample contains more recently listed firms. Average *Sales Growth* is around 12% and the *Leverage* ratio has a mean value of 0.18. In addition, *Big4 Auditor* has a mean value of 0.45, suggesting that only 45% of the sample firms are audited by one of the Big 4. These findings are also consistent with previous research conducted on Malaysian firms (Gul et al. 2016).

Figure 3.1 illustrates the trend of CEO-board cultural similarity from 2009 to 2016, showing that CEO-board cultural similarity slightly rises from an average of 67.5% in 2009 to 69.7% in 2016. **Figure 3.2** presents the CEO-board cultural similarity and firm value (*Tobin's Q*) over time. It reveals that firms with high cultural similarity have lower *Tobin's Q* than their counterparts with low cultural similarity. Finally, **Figure 3.3** plots the number of CEOs from different ethnic backgrounds by year. It shows that most of the CEOs in Malaysian firms are Chinese, followed by Malays, Indians, and then 'Others'.

In the Pearson correlation coefficient analysis, as shown in **Table 3.4**, the absolute values of the correlation coefficients between our variables are all below 0.5, indicating that multicollinearity is unlikely to be a severe problem in our study. We also compute the variance inflation factor (VIF) for all independent variables. The largest one is 1.34, far below a recommended threshold value of 10.00 for multiple regression models (Hair et al. 1998; Kennedy 1998), confirming that multicollinearity is not a serious problem in our study.

Table 3. 3: Summary statistics

This table reports summary statistics for CEO-board cultural similarity, firm performance, and control variables for a sample containing the non-financial firms listed in Bursa Malaysia. The final sample contains unbalanced panel data for 620 Malaysian firms for the period between 2009 and 2016. All variables are as defined in **Table 3.2**.

Variable	Obs.	Mean	Stdev.	Min.	0.25	Median	0.75	Max.
Cultural Similarity	5,670	0.69	0.23	0.00	0.57	0.75	0.83	1.00
Board Size	5,641	7.33	1.94	3.00	6.00	7.00	8.00	22.00
Board Independence	5,643	0.47	0.13	0.11	0.38	0.44	0.57	1.00
Board Meeting	5,637	5.40	1.97	0.00	4.00	5.00	6.00	27.00
Firm Size	6,008	2053.47	1323.94	1.00	868	2060.5	3237.5	4308
Leverage	5,694	0.18	0.23	0.00	0.03	0.15	0.29	10.9
R&D	5,992	0.01	0.08	-0.08	0.00	0	0.00	3.88
Sales Growth	5,590	0.12	1.46	-62.9	-0.09	0.04	0.17	49.58
Firm Age	6,049	28.75	20.56	1.00	25.00	25.00	37.00	188
Big4 Auditor	5,701	0.46	0.46	0.00	0.00	0.00	1.00	1.00
Tobin's Q	5,220	1.22	2.39	0.04	0.72	0.93	1.28	157.74
ROA	5,685	0.05	0.11	-0.88	0.01	0.05	0.10	0.96

Table 3. 4: Correlation matrix

This table reports the correlation matrix among the main variables used in our econometric analyses. Correlation coefficients significant at the 1% level or better are in bold. Refer to **Table 3.2** for detailed variable description.

	Variables	**1**	**2**	**3**	**4**	**5**	**6**	**7**	**8**	**9**	**10**	**11**	**12**
1	*Tobin's Q*	1											
2	*ROA*	-0.005	1										
3	*ROE*	-0.007	0.006	1									
4	*Cultural Similarity*	**-0.149**	0.005	0.021	1								
5	*Board Size*	**0.125**	-0.010	0.011	-0.006	1							
6	*Board Independence*	**-0.052**	-0.003	-0.004	**-0.069**	**-0.402**	1						
7	*Board Meeting*	-0.009	0.009	0.015	**-0.043**	**0.093**	**0.096**	1					
8	*Firm Size*	0.030	0.025	0.008	**-0.124**	**0.380**	**-0.075**	**0.222**	1				
9	*Leverage*	**-0.046**	-0.003	-0.007	-0.004	**0.102**	-0.014	**0.052**	**0.221**	1			
10	*Sales Growth*	**0.045**	-0.003	0.004	-0.005	-0.009	0.011	-0.002	-0.000	-0.012	1		
11	*Firm Age*	**-0.051**	0.006	0.017	**-0.087**	**0.118**	-0.014	**0.042**	0.295	0.006	**-0.040**	1	
12	*Big4 Auditor*	**0.070**	**0.037**	0.007	**-0.072**	**0.189**	**-0.095**	**0.062**	**0.442**	**0.077**	-0.002	**0.1953**	1

Figure 3. 1: Percentage of CEO-board cultural similarity from 2009 to 2016

This figure shows the percentage of CEO-board cultural similarity on the board over time between 2009 and 2016.

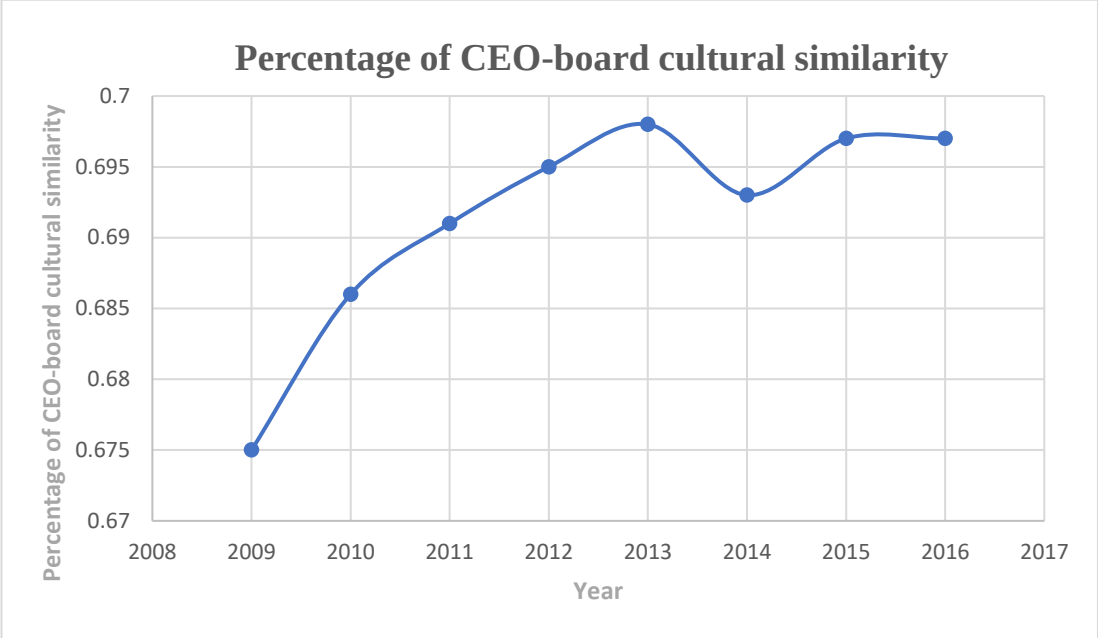


Figure 3. 2: CEO-board cultural similarity and firm value (Tobin's Q over time)

This figure shows time variation of annual average values of Tobin's Q for firms with high and low cultural similarity between the CEO and board of directors from 2009 to 2016.

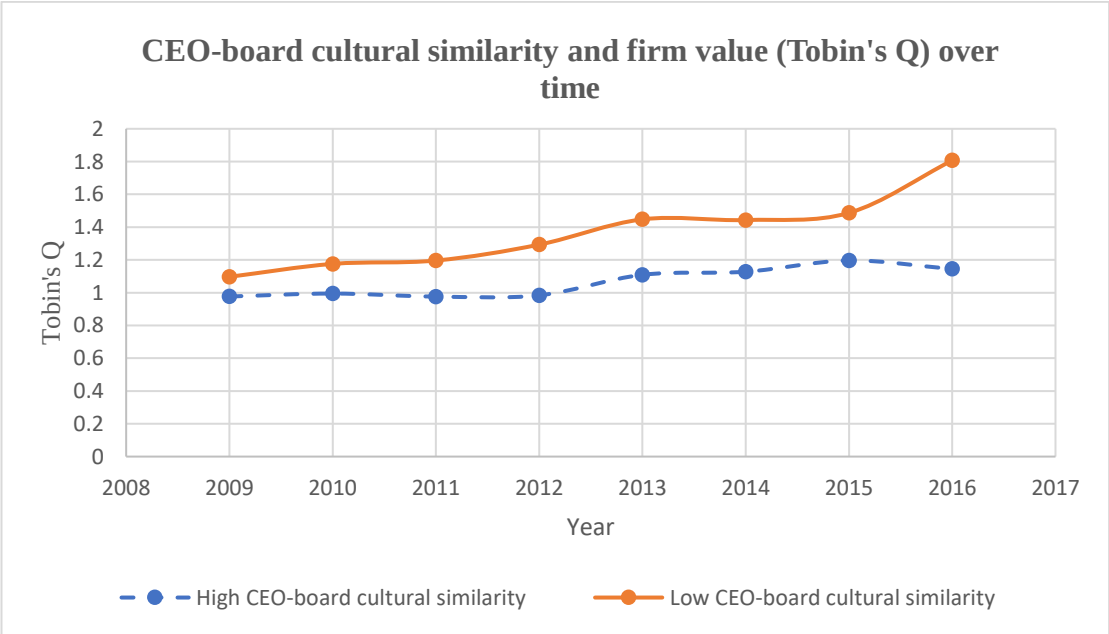
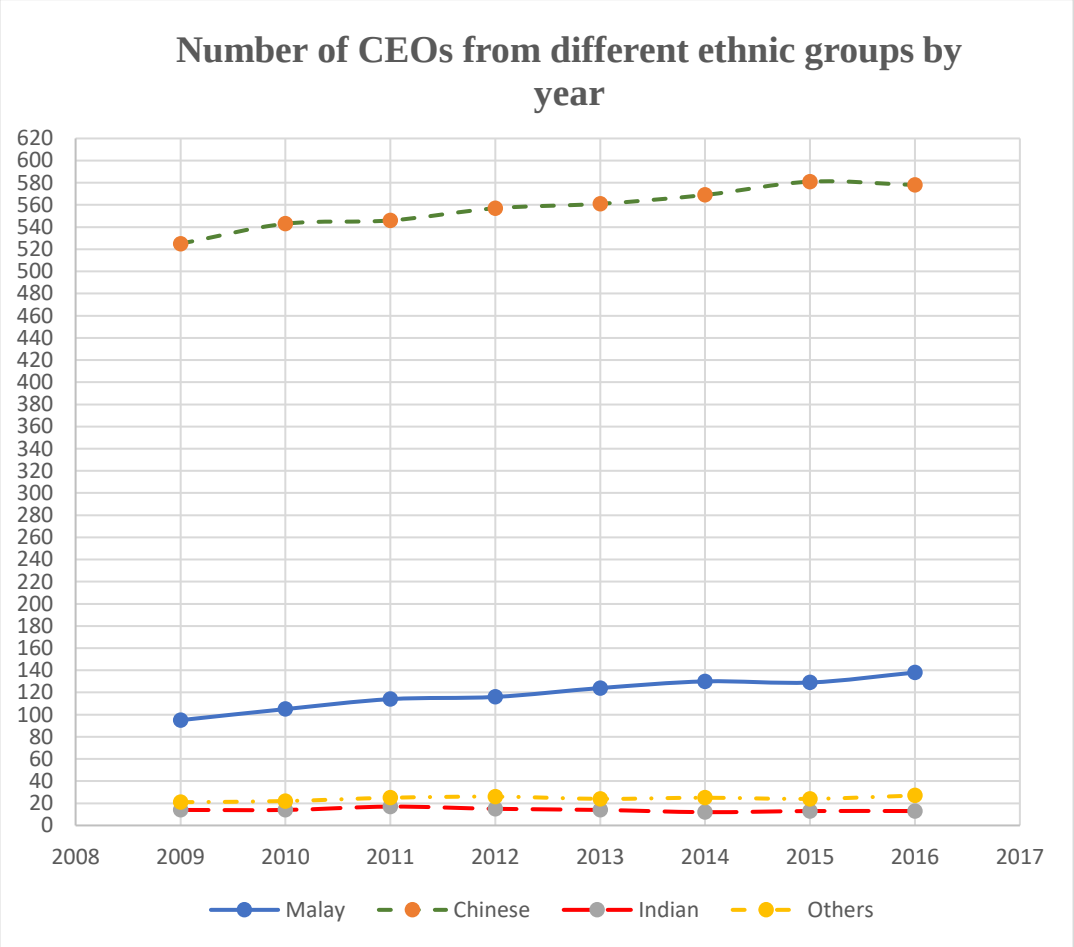


Figure 3. 3: Number of CEOs from different ethnic groups by year

This figure exhibits the number of CEOs from different ethnic background by year for a sample containing the non-financial firms listed in Bursa Malaysia. The final sample contains unbalanced panel data for 620 Malaysian firms for the period between 2009 and 2016. All variables are as defined in **Table 3.2.**



3.4 Empirical Results

To estimate the impact of cultural similarity between CEO and directors on firm value, we estimate the following OLS regression for firm *i* in year *t*:

$$Firm\ value_{it} = a_0 + a_1 Cultural\ Similarity_{it} + a_2 Board\ characteristics_{it} + a_3 Firm\ characteristics_{it} + Industy\ dummies + Year\ dummies + \varepsilon_{it} \quad \textbf{(3.1)}$$

where firm value is measured by *Tobin's Q*, CEO-Board cultural similarity (*Cultural Similarity*) is measured by the proportion of board directors with the same ethnicity as the CEO; *Board characteristics* variables (i.e. *Board Independence*, *Board Size*, and

Board Meeting); and the *Firm characteristics* variables (i.e. *Firm Size*, *Firm Age*, *Sales Growth*, *Leverage*, and *Big4 Auditor)* are control variables; *Industry dummies* based on the two-digit SIC industry classification are included to account for industry effects; *Year dummies* are also incorporated in the model to account for the effect of market-wide shocks on firm value. Standard errors are clustered at the firm level to account for the serial correlation of error terms.

3.4.1 Baseline results

To evaluate the effect of CEO-board cultural similarity on firm value, we begin the analysis by regressing *Tobin's Q* on *Cultural Similarity*. **Table 3.5** reports the estimates from our OLS regressions. In column (1), the coefficient on *Cultural Similarity*, as the only explanatory variable, is negative (b=-0.270) and significant at the 1% level. Column (2) shows similar results after firm characteristics are introduced (b=-0.214, p<.01). Column (3) presents test results after controlling for both board and firm characteristics. The inclusion of the two groups of control variables does not alter the sign or the significance of the *Cultural Similarity* (b=-0.218, p<.01), consistent with **Hypothesis 1b**. The economic magnitude is substantial. In terms of economic significance, a one-standard-deviation increase in cultural similarity is associated with a 6.14% decline in firm value. This evidence suggests that the costs and frictions on the alignment in cultural values between CEO and other directors outweigh the potential benefits of having cultural similarity between CEO and directors on corporate boards, and adds to the stream of literature on the impact of CEO-board similarities and social connections on firm value (Fracassi and Tate 2012; Lee et al. 2014; Goergen et al. 2015; Fan et al. 2019).

As for the control variables, we find that the coefficient on *Board Size* is positive and significant, indicating larger boards achieve higher valuations, which is consistent with prior studies (Pearce and Zahra 1992; Coles et al. 2008; Fauzi and Locke 2012). We also find that the coefficient on *Board Meeting* is positive and significant, implying board meeting is associated with higher firm value, whereas the coefficient on *R&D*, *Big4 Auditor* and *Sales Growth*, are respectively positive and significant, indicating that firms with higher R&D, audited by Big 4 auditing firms and with higher growth opportunities are associated with higher firm value, which is in line with Gul et al. (2016). Our results also consistent with the studies on the influence of similarities

between top managers and board of directors in the form of shared networks, similar regional, age, or educational background, or similar political orientation on firm performance (Hwang and Kim 2009; Lee et al. 2014; Goergen et al. 2015; Fan et al. 2019). These studies show that the similarities between CEO and other directors on corporate boards are associated with weaker governance and lower firm value.

Table 3. 5: CEO-board cultural similarity and firm value

This table reports the OLS estimation results of *Tobin's Q* on the measure of CEO-board cultural similarity, board characteristics, and firm characteristics for Malaysian non-financial listed firms in the sample period of 2009 to 2016. *Tobin's Q* is calculated as market value of assets over book value of assets. *Cultural similarity* is the proportion of board directors that share similar ethnicity with the CEO. All other variables are defined in **Table 3.2**. Standard errors are clustered at the firm level and t-statistics are reported in parentheses. ***, **, * denote statistical significance at the 1%, 5%, and 10% level, respectively.

	Tobin's Q		
	(1)	**(2)**	**(3)**
Cultural Similarity	-0.270***	-0.214***	-0.218***
	(-3.773)	(-2.963)	(-3.168)
Board Size			0.224***
			(3.511)
Board Independence			-0.115
			(-0.918)
Board Meeting			-0.070*
			(-1.796)
Firm Size		0.017	0.009
		(1.180)	(0.677)
Leverage		-0.009	-0.009
		(-0.853)	(-0.868)
R&D		25.353*	29.571**
		(1.764)	(1.983)
Sales Growth		0.673***	0.740***
		(2.766)	(2.804)
Firm Age		0.002	-0.002
		(0.077)	(-0.077)
Big4 Auditor		0.080**	0.074**
		(2.392)	(2.239)
Intercept	0.068	-119.965*	-139.885**
	(0.467)	(-1.810)	(-2.035)
Industry FE	Yes	Yes	Yes
Year FE	Yes	Yes	Yes
Observations	5,157	4,426	4,392
R-squared	0.2073	0.2301	0.2482

3.4.2 Robustness checks

After presenting the baseline evidence, we next verify the robustness of our main results to alternative variable definitions, to alternative model specifications, and to endogeneity concerns.

3.4.2.1 Alternative measurements and specifications

Table 3.6 reports the coefficients of our variable of interest, C*ultural Similarity*, obtained from various alternative measurements and specifications. Row (0) shows the results from our baseline specifications in **Table 3.5** for comparison.

First, following prior research (e.g., Hwang and Kim 2009; Fracassi and Tate 2012; Lee et al. 2014; Goergen et al. 2015), we use return on assets (*ROA*), measured as income before extraordinary items scaled by average total assets in year *t* and *t*-1, as an alternative measure of firm performance. As row (1) shows, we continue to find a negative and significant relation between CEO-board cultural similarity and operating performance. The results also hold when we control for board and firm characteristics.

Next, we use the firm's adjusted stock return and market-to-book value (*MTB*) as alternative measures of market-based firm performance in our main analyses. We again find a consistently negative relation between CEO-Board cultural similarity and market-based firm performance (see rows (2) and (3)). Similar results are obtained when *Tobin's Q* without the natural-logarithm transformation is regressed on the independent variables (see row (4)).

In row (5) of **Table 3.6,** we control for CEO duality, which is coded as a dummy variable equal to one if the CEO also serves as chair of the board. We examine whether CEO-cultural-tied directors yield greater board power and their effect is robust when the CEO also serves as board chair. As shown in row (5), our result continues to hold when we control for *CEO Duality* in our baseline regressions.

Next, we rerun our baseline regression by controlling for profitability (*ROA*), the ratio of net income over total assets at the end of the year, as a firm's profitability affects its market value (Yermack 1996). Again, our conclusions remain unchanged. Furthermore, to correct statistical averages that may consist of clear imbalances due to the outliers in the dataset as well as to control for industry characteristics not captured by other explanatory variables (Flannery and Rangan 2006; Hwang and Kim 2009), rows (7) and (8) adjust the variables by industry means and medians, respectively, showing that our results continue to hold. Next, we regress our main dependent variable, *Tobin's Q*, on the lagged values of our explanatory variables as these variables are largely predetermined (Boone et al. 2007; Faleye 2015); the results, shown in row (9), are qualitatively similar to those reported in **Table 3.5**.

Next, to mitigate the concern of specific estimation method error, we rerun our regressions by using random effects as motivated and used in the previous literature (Andres 2008). Row (10) shows that the random effect estimates generate consistent results with our previous findings. In row (11), the estimation results from the quantile regressions, which are less influenced by outliers, also hold.

Further, we consider two alternative measures of CEO-board cultural similarity. First, as opposed to using a fraction of CEO-board cultural similarity, we construct and use a dummy variable that equals one if *Cultural Similarity* is above the sample mean, and zero otherwise. Second, we compute the fraction of CEO-audit committee cultural similarity as a second alternative measure. As rows (13) and (14) show, the coefficients for these alternative measures are similarly negative and significant, consistent with our main findings. Finally, row (15) confirms the validity of our results after further excluding utility firms, which are heavily regulated, from our estimation.

Table 3. 6: Robustness tests

This table reports the coefficients of our variable of interest, CEO-board cultural similarity (*Cultural Similarity*) from alternative specifications of the regressions. The main specification, shown in row (0), is the main regression on the full sample with the complete set of controls, as shown in column (3) of **Table 3.5**. Standard errors are clustered at the firm level and t-statistics are reported in parentheses. ***, **, * indicate significance at the 1%, 5% and 10% level, respectively.

		Cultural Similarity			
		Coef.	***t-value***	***S.E***	***Obs.***
(0)	Main specification	-0.218***	-3.17	0.068	4,392
(1)	Return on asset as alternative measure of firm performance	-0.021**	-2.03	0.010	4,621
(2)	Stock return as alternative measure of firm value	-0.072*	1.89	0.078	4,200
(3)	Market-to-book ratio as alternative measure of firm value	-0.248**	-2.31	0.107	4,603
(4)	Tobin's Q (without log) as alternative measure of firm value	-0.435***	-2.97	0.146	4,392
(5)	Controlling for CEO duality	-0.211***	-3.05	0.069	4,391
(6)	Controlling for profitability (*ROA*)	-0.230***	-3.48	0.067	4,384
(7)	Adjusting variable by the industry mean	-0.376**	-2.54	0.148	4,392
(8)	Adjusting variable by industry median	-0.419***	-2.86	0.147	4,392
(9)	Lagged values of explanatory variables	-0.239***	-3.33	0.072	3,819
(10)	Random effect regression, robust, clustered at the firm level	-0.104**	-2.18	0.048	4,392
(11)	Quantile regression	-0.183***	-6.43	0.029	4,392
(12)	CEO-board cultural similarity dummy as alternative variable of interest	-0.079***	-2.85	0.028	4,392
(13)	CEO-audit committee cultural similarity as alternative variable of interest	-0.008***	-2.61	0.002	4,374
(14)	Excluding utility companies and regulated companies	-0.179***	-2.70	0.066	3,847

3.4.2.2 Endogeneity

Our baseline regression results show a negative relation between CEO-board cultural similarity and firm value. Nevertheless, the results may be driven by endogeneity. For instance, a firm's decision to appoint a CEO with a similar cultural background to other directors is not randomised, and, hence, our results may subject to potential self-selection bias. In addition, it is plausible that some omitted variables that simultaneously affect the appointment of a CEO with similar cultural background to other board members and firm value drive our results. Furthermore, there is a reverse causality concern, as high-performing firms may also adopt strategies that lower CEO-board cultural similarity, or vice versa. We address these potential endogeneity issues in three ways (i.e., firm fixed effect, propensity score matching, and instrumental variables approach).

A) Controlling for firm fixed effects

To alleviate potential problems that could arise from omitted time-invariant firm characteristics, we re-estimate model (**3.1)** with the inclusion of firm fixed effects.

Table 3.7 reports the results. Column (1) reports the results with *Cultural Similarity* as the only explanatory variable in the regression. Consistent with the earlier finding, the coefficient on *Cultural Similarity* is negative (b=-0.081) and significant at the 1% level, indicating that CEO-board cultural similarity is associated with lower firm value.

In column (2), the coefficient on *Cultural Similarity* remains negative and significant (b=-0.081, p<.05) after controlling for firm characteristics. When controlling for both firm and board characteristics in column (3), the coefficient on *Cultural Similarity* remains negative (b=-0.065*)*, but only significant at the 10% level, implying that CEO-board cultural similarity reduces firm value, which is consistent with our main results in **Table 3.5**. Although the results show a little loss in statistical significance, the fixed effects estimates suggest that our results are not driven by an omitted variable bias.

Table 3. 7: Controlling for firm fixed effects

This table reports the OLS estimation results of *Tobin's Q* on a measure of CEO-board cultural similarity, and board and firm characteristics for Malaysian non-financial listed firms in the sample period of 2009 to 2016. *Tobin's Q* is calculated as market value of assets over book value of assets. The *Cultural Similarity* is the proportion of board directors that share similar ethnicity with the CEO. All other variables are defined in **Table 3.2**. ***, **, * indicate statistical significance at the 1%, 5%, and 10% level, respectively.

	Tobin's Q		
Cultural Similarity	-0.081**	-0.093**	-0.065*
	(-2.049)	(-2.343)	(-1.654)
Board Size			0.079**
			(2.430)
Board Independence			-0.045
			(-0.765)
Board Meeting			-0.048**
			(-2.296)
Firm Size		-0.115***	-0.050***
		(-7.914)	(-3.382)
Leverage		0.015***	0.007
		(2.945)	(1.455)
R&D		-8.870	-7.504
		(-1.170)	(-1.024)
Sales Growth		0.489**	0.399*
		(2.163)	(1.820)
Firm Age		-0.029	-0.058
		(-0.594)	(-1.216)
Big4 Auditor		0.004	-0.003
		(0.176)	(-0.121)
Intercept	-0.009	39.370	33.116
	(-0.323)	(1.126)	(0.981)
Firm FE	Yes	Yes	Yes
Year FE	Yes	Yes	Yes
Observations	5,157	4,426	4,392
R-squared	0.0315	0.0483	0.0390

B) Propensity score matching

We also employ a matching approach and apply propensity score matching techniques to mitigate concerns relating to self-selection (Rosenbaum and Rubin 1983; Shipman et al. 2017) and 'sample selection bias' that is triggered by observable factors (Dehejia and Wahba 2002). For instance, CEOs with high demographic similarity to directors are more prone to appoint similar directors (e.g., directors who share the same ethnicity) (Westphal and Zajac 1995) which affects the firm value.

We compare the firm value in firms with high cultural similarity (i.e., treatment firms) and a sample of control firms with low cultural similarity (i.e., control firms). We define the treatment firms as firms with an above-sample mean fraction of CEO-board cultural similarity and control firms as firms with a below-sample-mean fraction of CEO-board cultural similarity.

The propensity score matching method proceeds in two steps. First, we estimate a probit[9] model using the full sample to compute the probability (i.e., the propensity score) that a firm with a set of firm-level characteristics is run by the treatment firms. We use the same controls as those included in the baseline regression. The probit regression results are reported in column (1) in Panel A of **Table 3.8**. We find that firms with high cultural similarity are smaller, younger, more leveraged, and have smaller board size than their counterparts with low cultural similarity.

To ensure that firms in the treatment sample and control sample are comparable, we employ the nearest neighbour approach. Specifically, each firm with high cultural similarity is matched to a firm with a low cultural similarity that has the closest propensity score. In our matching, we require the maximum difference between the propensity scores of the firm with high and that with low cultural similarity to not exceed 0.1% in absolute value.

Next, we employ two diagnostic analyses to verify that firms in the treatment and control groups are indistinguishable in terms of observable characteristics. First, we re-estimate the probit model for the post-match sample. Column (2) in Panel A shows that all of the estimated coefficients are statistically insignificant, implying the absence of any distinguishable trends in firm value between the two groups. In addition, the estimated coefficients in column (2) are smaller in magnitude than those in column (1), signifying that the decrease in statistical significance is not simply driven by reduced sample size. Lastly, **Table 3.8** shows a decrease in pseudo-R-squared from 0.026 for the pre-match sample to 0.002 for the post-match sample. This implies that propensity score matching eliminates all observable differences other than those related to cultural similarity.

[9] We also use a logit model in the first step as an alternative test and the results are qualitatively similar.

Second, we examine the differences for each observable characteristic between the treatment firms and the matched control firms. All univariate difference tests in Panel B of **Table 3.8** are statistically insignificant, indicating that the differences in firm value between the treatment and control groups are only due to the presence of cultural similarity.

Panel C of **Table 3.8** presents the propensity score matching estimates. The results indicate that there are significant differences, at the 1% level, in firm value between firms with high and those with low cultural similarity

Finally, we re-estimate the baseline model by using treatment and matched control sample and reports the result in Panel D of **Table 3.8**. The results show that the coefficient on *Tobin's Q* is significantly negative at the 1% level, suggesting a negative association between cultural similarity and firm value. Thus, the propensity score matching results are consistent with those in the baseline specification, implying that our main findings are unlikely to be influenced by omitted variables related to nonlinear forms of our control variables.

Table 3. 8: Propensity score matching estimates

This table reports the propensity score matching estimation results. Panel A reports estimates from the probit model used to estimate propensity scores. The dependent variable is a dummy variable that equals one for firms with high *Cultural Similarity*, and zero otherwise. We define a firm with high CEO-board cultural similarity (treatment firms) if it has an above-sample mean fraction of CEO-board cultural similarity and a firm with low CEO-board cultural similarity (control firms) if it has below-sample-mean fraction of CEO-board cultural similarity. All independent variables are defined in **Table 3.2**. Industry dummies are constructed based on the two-digit SIC code classification. Panel B reports the univariate comparisons of firm characteristics and board characteristics between treatment group and control group. Panel C reports the average treatments estimates. Panel D reports the regression results using PSM procedure. ***, **, and * indicate significance at the 1%, 5%, and 10% level, respectively.

Panel A: Pre-match propensity score regression and post-match diagnostic regression

	High Cultural Similarity Dummy	
	(1)	**(2)**
	Pre-Match	**Post-Match**
Board Independence	-0.131	-0.085
	(-1.497)	(-0.669)
Board Size	-0.504***	-0.133
	(-3.073)	(-0.583)
Board Meeting	0.095	0.043
	(1.477)	(0.449)
Firm Size	-0.134***	0.024
	(-8.945)	-1.103
Leverage	0.028**	-0.018
	-2.198	(-1.008)
R&D	-22.465	-41.844
	(-0.791)	(-1.136)
Sales Growth	-1.589	-0.657
	(-1.084)	(-0.590)
Firm Age	-0.083***	-0.042
	(-2.789)	(-1.013)
Big4 Auditor	-0.006	-0.053
	(-0.133)	(-0.921)
Intercept	112.252	195.867
	-0.858	-1.155
Observations	4,638	3,389
Pseudo R^2	0.0264	0.002
Industry FE	Yes	Yes
Year FE	Yes	Yes

Panel B: Differences in the firm and board characteristics

	Firm-year obs. with high CEO-board cultural similarity (N=2212)	Firm-year obs. with low CEO-board cultural similarity (N=2180)	Difference	*t*-stat
Board Independence	1.9510	1.9536	-0.0026	-0.35
Board Size	0.4599	0.4617	-0.0018	-0.49
Board Meeting	1.6408	1.6346	0.0062	0.71
Firm Size	5.6624	5.6354	0.0270	0.61
Leverage	-2.2090	-2.1701	-0.0389	-0.90
R&D	4.6052	4.6053	-0.0001	-1.80
Sales Growth	4.6058	4.6061	-0.0003	-0.48
Firm Age	3.1389	3.1608	-0.0219	-1.11
Big4 Auditor	0.4299	0.4435	-0.0136	-0.91

Panel C: Propensity score matching estimator

Variables	Firm-year obs. with high CEO-board cultural similarity	Firm-year obs. with low CEO-board cultural similarity	Difference	T-stat
Tobin's Q	-0.0724	0.0397	-0.1121***	-7.28
ATT	-0.0724	0.0155	-0.0879***	-4.04

Panel D: The regression results using PSM procedure

	Tobin's Q
Cultural Similarity	-0.081***
	(-2.802)
Board Size	0.203***
	(3.071)
Board Independence	-0.089
	(-0.754)
Board Meeting	-0.050
	(-1.322)
Firm Size	0.011
	(0.761)
Leverage	-0.011
	(-0.990)
R&D	27.116*
	(1.907)
Sales Growth	1.786
	(1.512)

Firm Age	-0.008
	(-0.294)
Big4 Auditor	0.071**
	(2.190)
Intercept	-133.607**
	(-2.016)
Industry FE	Yes
Year FE	Yes
Observations	3,692
R-squared	0.2325

C) The instrumental variables approach

Another potential source of endogeneity is simultaneity; that is, the cultural similarity between CEO and other directors on a board may be determined by the firm's recruitment policies. Specifically, the negative association between cultural similarity and firm value may arise from the possibility that low-performing firms recruit CEOs with a similar background to other board members. A potential solution to this problem is to use an instrumental variables approach, which also addresses potential errors-in-variables issues (Roberts and Whited 2013). We employ a two-stage model using two instrument variables that work better in Malaysian context. Particularly, we employ two instruments that are unlikely to exert an effect on accrual-based earnings management but should have an indirect relationship through their effects on CEO-board cultural similarity.

The first instrument we employ is a dummy variable for whether a firm is headquartered outside of a large metropolitan city. Meanwhile, we use ethnic heterogeneity index of the Malaysian states as a second variable. One of the motivations selecting these instruments is that we expect firms headquartered in the small towns or outside of a large metropolitan area to be less culturally diverse than firms headquartered in larger city. We also expect that firms that located or headquartered in Malaysian states that have lower ethnic heterogeneity index tend to be less culturally diverse than firms located or headquartered in states that have higher ethnic heterogeneity. This argument is consistent with Anderson et al. (2011), Frijns et al. (2016) and Masulis et al. (2012) concerning their instruments which are mainly focused on the location of firms' headquarters and country heterogeneity as their instruments of board heterogeneity or cultural diversity.

Column (1) in **Table 3.9** reports the results of the first-stage regressions where the dependent variable is the fraction of CEO-board cultural similarity, *Cultural Similarity*, estimated by the two-stage least squares. It shows that coefficients on both instrumental variables are positive and significant at the 1% level, suggesting that our instruments are valid. The reported high F-statistics well exceed the threshold value of 10 suggested by Staiger and Stock (1997) and the *p*-value of the Cragg-Donald's Wald *F* weak-instrument test statistic is 0.000, rejecting the null hypothesis that the instruments are weak (Cragg and Donald 1993; Stock and Yogo 2005). In addition, Hansen's J overidentification test shows a *p*-value of 0.101, implying that the two instruments are valid, or uncorrelated with the error term (Hansen 1982).

Column (2) reports the second-stage regression results. We find that the estimate for the fitted *Cultural Similarity* is significantly negative, indicating that the relation obtained from the OLS regression can be interpreted in a causal way. That is, the higher the cultural similarity the lower the firm value. We also note that the estimated coefficients from the instrumental variable approach are slightly higher than their counterparts from the OLS regressions. This can be attributed to the instrumental variable approach reducing the errors-in-variables bias and, therefore, reconfirming the strong negative association between cultural similarity and firm value.

Table 3. 9: Instrumental variables estimation

This table reports instrumental variables regression estimation results. Column (1) reports the first-stage results of the 2SLS regressions with *Cultural Similarity* as the dependent variable. *Tobin's Q* is calculated as market value of assets over book value of assets. *Cultural Similarity* is the proportion of board directors that share similar ethnicity with the *CEO*. *Malaysia Small Town* is a dummy variable which equals one if a firm is headquartered outside of a large metropolitan area and zero, otherwise. *State Ethnic Heterogeneity* is a *dummy* variable which equals one if a firm is headquartered in a state with lower state ethnic heterogeneity index in Malaysia and zero, otherwise. Colum (2) report the second-stage results from 2SLS regressions for Tobin's Q, respectively. All other variables are defined in **Table 3.2**. Standard errors are clustered at the firm level and t-statistics are reported in parentheses. ***, **, * indicate significance at the 1%, 5% and 10% level, respectively

	First stage	**Second stage**
	Cultural Similarity	***Tobin's Q***
	(1)	**(2)**
Malaysia Small Town	**0.041*** **	
	(4.63)	
State Ethnic Heterogeneity	**0.054*** **	
	(2.81)	
Cultural Similarity		-2.016***
		(-4.380)
Board Size	0.024	0.282***
	(1.47)	(5.879)
Board Independence	-0.134***	-0.357***
	(-4.27)	(-3.258)
Board Meeting	0.014	-0.038
	(1.12)	(-1.066)
Firm Size	-0.018***	-0.030**
	(-5.94)	(-2.430)
Leverage	0.002	-0.004
	(0.82)	(-0.618)
R&D	-5.112	27.061*
	(-0.93)	(1.753)
Sales Growth	-0.016	0.624
	(-0.09)	(1.262)
Firm Age	-0.040***	-0.075***
	(-6.51)	(-2.859)
Big4 Auditor	0.011	0.090***
	(1.37)	(3.876)
Intercept	24.398	-126.287*
	(0.96)	(-1.774)
Industry FE	Yes	Yes
Year FE	Yes	Yes
Observations	3,903	3,903
R-squared	0.135	
Cragg–Donald Wald *F* statistic	18.50	
Hansen J *p*-value	0.101	

D) Heckman selection model

A firm's decision to appoint a CEO with higher cultural ties with board of directors may be non-random and this may cause a self-selection bias. Thus, to address this concern, we conduct the Heckman two-step sample selection model as robustness check. In the first stage model, we compute the inverse Mills ratio from a probit model that captures the determinants of firms appointing CEO with similar cultural ties with board of directors. In particular, this probit model controls for a dummy variable (*Malaysia Small Town*) for whether a firm is headquartered outside of a large town in Malaysia. The motivation to use this exogenous variable is that we assume firms headquartered in these areas are to be less culturally diverse than firms headquartered in large towns (Anderson et al. 2011; Frijns et al. 2016). Furthermore, Heckman's estimator requires exogenous variable that is correlated with a firm's propensity to appoint CEO with similar cultural background with board of directors, but not with firm value. Thus, the *Malaysia Small Town* is likely to be an important factor for a firm to appoint CEO that has higher cultural similarity with board of directors.

We also control for *Board Size*, *Board Independence*, *Board Meeting*, *Firm Size*, *Leverage*, *R&D*, *Sales Growth*, *Firm Age* and *Big4 Auditor*. In the second stage, we include the inverse Mills ratio which is generated from first stage into the regression model as an additional control variable to control for the potential sample selection bias. The results of the first-step regression in Column (1) of **Table 3.10** show that *Malaysia Small Town*, *Leverage*, *Board Size* have significant and positive impacts on the CEO-board cultural similarity, whereas *Board Independence*, *Firm Size* and *Firm Age* have significantly negative impacts.

The results of the second-step regression in Column (2) of **Table 3.10** show that the coefficient on *Cultural Similarity* remain significantly negative. The coefficient on *Inverse Mills Ratio* is significant and positive, signifying that the unobserved factors that motivate firms to appoint CEOs with similar cultural background are positively associated to firm value.

Overall, our reported findings in **Table 3.10** are qualitatively similar to our results reported under the main analysis and hence implying that our results reported under the main analysis do not appear to be driven sample selection bias.

Table 3. 10 : Heckman two-stage analysis

This table reports the regression results of Heckman model. The first step is a probit model with a binary cultural similarity dummy. *Dummy Cultural Similarity* equals one if the firm has an above-sample mean fraction of CEO-board cultural similarity and zero, otherwise. *Malaysia Small Town* is an exogenous variable, which equals one if the firm is headquartered in small towns and zero, otherwise. The second stage is ordinary least square regression of the impact of CEO-board cultural similarity on firm value. *Inverse Mills Ratio* is generated from the first step and included in the second step of this model. All other variables are defined in **Table 3.2**. Standard errors are clustered at the firm level and t-statistics are reported in parentheses. ***, **, * denote statistical significance at the 1%, 5%, and 10% level, respectively.

	First-step regression	Second-step regression
	Dummy Cultural Similarity	***Tobin's Q***
	(1)	(2)
Cultural Similarity		-0.264***
		(-3.188)
Malaysia Small Town	0.338***	
	(7.836)	
Board Size	0.224**	0.175***
	(2.480)	(3.665)
Board Independence	-0.495***	-0.372***
	(-2.948)	(-3.860)
Board Meeting	0.080	0.049
	(1.214)	(1.435)
Firm Size	-0.099***	-0.025**
	(-6.459)	(-2.329)
Leverage	0.026**	0.011
	(2.025)	(1.537)
R&D	-17.702	30.463**
	(-0.622)	(2.239)
Sales Growth	-1.426	0.593
	(-0.963)	(1.290)
Firm Age	-0.100***	-0.037**
	(-3.293)	(-2.035)
Big4 Auditor	0.068	0.001
	(1.576)	(0.041)
Inverse Mills Ratio		0.431***
		(3.707)
Intercept	88.733	-142.978**
	(0.677)	(-2.280)
Industry FE	Yes	Yes
Year FE	Yes	Yes
Observations	4,472	4,472
Pseudo R2	0.028	
Adjusted R2		0.238

3.4.3 Additional analyses

3.4.3.1 Board independence and firm value

Board independence is one of the most important internal mechanisms that enhance governance quality. Major rules and regulations of corporate-governance codes of conduct worldwide typically require company boards to be independent. Most of these rules and regulations define board independence as a state in which all or a majority of members of a board of directors do not have familial, financial, or any other overt ties to the firm or top management. However, previous studies have reported that conventionally defined board independence is insufficient due to the presence of social ties and pre-existing network connections between CEOs and independent directors, which are associated with weaker internal governance (Hwang and Kim 2009; Krishnan et al. 2011) and reduced firm value (Fracassi and Tate 2012).

In this section, we suggest that conventionally defined board independence may be irrelevant and weak in explaining firm value as the Malaysian corporate setting and economic activities are usually characterised by relationship-based principles, where economic agents depend heavily on social ties and/or connection. Furthermore, in the Malaysian setting, ethnic considerations have emerged to influence economic activities, social and governance systems. As Malaysia is a multicultural country, with a variety of ethnic groups, each with their own culture, the setting as well as the launch of the affirmative policy may be having a significant influence on the composition of boards of directors as well as the effectiveness of board independence.

Thus, we propose a culturally-adjusted measure of board independence which to address whether firms with independent directors who are culturally independent of the CEOs reduce agency cost and eventually firm value.

We construct a conventionally independent board dummy (*CIB*) that equals one if there is a majority of directors who are classified as independent based on conventional definitions (i.e., based on the Malaysian Code on Corporate Governance), and zero otherwise. To incorporate cultural similarity into the measurement of board independence, we construct a culturally adjusted independent board dummy (*AIB*) that equals one when more than half of the board comprises directors who are both

conventionally and culturally independent (i.e., those who have no cultural ties with the CEO), and zero otherwise. We perform the baseline firm-value tests regressing *Tobin's Q* on the board independence measures, firm controls, and industry and year fixed effects and report these estimation results in **Table 3.11**.

Column (1) shows that the coefficient on *CIB* is statistically insignificant (b=-0.014*;* t=-0.461). In column (2), where the conventional measure is replaced by the culturally adjusted measure, we find that the coefficient on *AIB* is positive and statistically significant at the 5% level (b=0.067*;* t=2.175). The economic magnitude is substantial. The point estimate of 0.067 indicates that, for a one-standard-deviation increases in *AIB*, 0.74, *Tobin's Q* is increased by 0.050, which corresponds to 4.098% of its sample average (1.22).

These findings suggest that cultural independence between the CEO and the board has a beneficial effect on the firm value above and beyond that of the conventional board-independence measure. In other words, the positive effect of board independence on firm value is particularly strong when directors are truly independent, i.e., they do not have any formal or cultural ties with the CEO.

As for the control variables, we find that the coefficient on *Board Size* is positive and significant, indicating that larger boards achieve higher valuations, which is consistent with prior studies (Pearce and Zahra 1992; Coles et al. 2008; Fauzi and Locke 2012). We also find that the coefficient on *Board Meeting* is positive and significant, implying that board meeting is associated with higher firm value, whereas the coefficients on *R&D*, *Big4 Auditor* and *Sales Growth*, are respectively positive and significant, indicating that firms with higher R&D, audited by Big 4 auditing firms and with higher growth opportunities are associated with higher firm value, which is in line with Gul et al. (2016).

Table 3. 11: Board independence and firm value

This table exhibits OLS regression estimation results of *Tobin's Q* on board and firm characteristics of Malaysian non-financial listed firms in the sample period of 2009 to 2016. *Tobin's Q* is calculated as market value of assets over book value of assets. *Conventionally Independent Board Dummy (CIB*) is classified as a dummy that equals one if a majority of directors are classified as independent as specified by current regulations, and zero otherwise. *Culturally Adjusted Independent Board Dummy (AIB*) is a dummy that equals one if the board consists of majority of directors who are both formally and culturally independent, and zero otherwise. All other variables are defined in **Table 3.2**. Standard errors are clustered at the firm level and t-statistics are reported in parentheses. ***, **, * denote statistical significance at the 1%, 5%, and 10% level, respectively.

	Tobin's Q	
	(1)	**(2)**
Conventionally Independent Board Dummy (CIB)	-0.014	
	(-0.461)	
Culturally Adjusted Independent Board Dummy (AIB)		0.067**
		(2.175)
Board Size	0.230***	0.228***
	(3.800)	(3.850)
Board Meeting	-0.076*	-0.073*
	(-1.921)	(-1.886)
Firm Size	0.014	0.012
	(0.971)	(0.839)
Leverage	-0.010	-0.010
	(-0.935)	(-0.927)
R&D	30.777*	29.996*
	(1.949)	(1.925)
Sales Growth	0.744***	0.742***
	(2.769)	(2.903)
Firm Age	0.008	0.004
	(0.280)	(0.135)
Big4 Auditor	0.073**	0.075**
	(2.225)	(2.284)
Intercept	-145.690**	-142.120**
	(-2.001)	(-1.979)
Industry FE	Yes	Yes
Year FE	Yes	Yes
Observations	4,401	4,401
R-squared	0.2388	0.2413

3.4.3.2 Board monitoring

Having established the evidence on the impact of CEO-board cultural similarity on firm value as well as board independence, we further analyse the effect of CEO-board similarity on the board monitoring effectiveness. First, we will measure whether the

similarity affects the frequency of monitoring activities and information exchange as measured by board meeting frequency. Second, we will measure whether the negative relation between cultural similarity and firm value differs among dependent (executive) or independent directors. As important management monitors, independent directors play a significant role in monitoring the CEOs, and thus we expect that the negative effect of cultural similarity on firm value is more concentrated among the independent directors.

A) Board meeting frequency

Board meeting frequency has also been commonly used in the corporate-governance literature as a proxy for increased board vigilance and monitoring (Carcello et al. 2002; Linck et al. 2008) as well as for board strategy control (Vafeas 1999). In fact, board meetings appear as a channel and medium for the directors to coordinate and perform their tasks accordingly as well as a principal avenue to participate effectively in overseeing management. Thus, the frequency of board meetings also represents the frequency of monitoring activities and information exchange.

The extant literature shows that social ties between CEOs and board of directors affect various organisational outcomes. Several studies focus on how social ties influence firm performance (Schmidt 2015; Gompers et al. 2016), selection of directors (Westphal and Zajac 1995), turnover (Hwang and Kim 2009; Nguyen 2012), and compensation (Hoitash 2011; Horton et al. 2012). However, this stream of research does not investigate the impact of social ties on the board activities, such as board meetings, which Vafeas (1999) and Brick and Chindambaran (2010) consider to be one of the best proxies for both the interaction between board members and the management and the monitoring and advising role of the board of directors

Thus, analysing board meeting frequency helps to shed some light on the monitoring effectiveness of boards of directors in the presence of social ties between board members and top management. Specifically, we postulate that a greater cultural similarity between CEO and board of directors may result in less monitoring. This is because, when CEO and board of directors share similar beliefs and values, they develop a high level of social cohesion and trust that could affect their communication as well as the information flow. Moreover, the CEO-board cultural similarity can reduce meeting frequency by stimulating mutual understanding and facilitating

information sharing and decision-making. On the other hand, a high level of cultural differences between the CEO and the board members can increase meeting frequency by making information exchange and decision-making harder.

Following the prior literature (e.g., Vafeas 1999; Adams 2003; Brick and Chidambaram 2010), we use the number of board meetings as a proxy for board monitoring intensity. According to the Malaysian Code of Corporate Governance 2007, Malaysian public listed firms are required to disclose the number of yearly board meetings held and information on director attendance.

Table 3.12 reports the OLS and firm fixed effect regression results for board meetings on the number of board meetings on board and firm characteristics. Column (1) exhibits our OLS estimation and shows that the coefficient on *Cultural Similarity* is not significant, implying that CEO-board cultural similarity is not associated with the number of board meetings. Nevertheless, we repeat the regression by using the fixed effect model, which controls for unobserved firm heterogeneity. Column (2) shows our fixed effect regression results and finds that the coefficient on *Cultural Similarity* is negative (*b*=-0.068*)* and significant at the 5% level, implying that the CEO-board cultural similarity is associated with the reduced monitoring needs. This evidence suggests that cultural similarity between the CEO and other board members reduces the frequency of board meetings and, therefore, decreases board vigilance and monitoring.

As for the control variables, we find that the coefficient on *Sales Growth* is negative and significant, indicating that firms with higher growth opportunities are associated with reduced monitoring needs. We also find that the coefficient on *Firm Age* is positive and significant, implying that the more mature firms are associated with greater monitoring needs. Our results are consistent with Goergen et al. (2015).

Table 3. 12: Cultural similarity and the number of board meetings

This table reports the OLS and fixed effect estimation results of the number of board meetings on board and firm characteristics. *Cultural Similarity* is the proportion of board directors that share similar ethnicity with the CEO. *Board Monitoring* is the number of board meetings held during the fiscal year. All other variables are defined in **Table 3.2**. Standard errors are clustered at the firm level and t-statistics are reported in parentheses. ***, **, * indicate significance at the 1%, 5% and 10% level, respectively

	Board Monitoring	
	(1)	**(2)**
	OLS	**Fixed effect**
Cultural Similarity	0.022	-0.068**
	(1.139)	(-2.281)
Board Size	0.088***	0.026
	(4.443)	(1.028)
Board Independence	0.290***	0.026
	(7.760)	(0.578)
Firm Size	0.035***	0.007
	(9.635)	(0.668)
Leverage	-0.001	0.001
	(-0.395)	(0.182)
R&D	6.008	3.935
	(0.902)	(0.683)
Sales Growth	-0.277	-0.446**
	(-1.209)	(-2.568)
Firm Age	0.008	0.207***
	(1.055)	(5.667)
Big4 Auditor	-0.003	0.012
	(-0.269)	(0.695)
Intercept	-25.400	-15.145
	(-0.828)	(-0.570)
Industry FE	Yes	Yes
Year FE	Yes	Yes
Observations	4,638	4,638
R-squared	0.1448	0.0263

B) Independent vs dependent (executive) directors

As an additional test of the relevance of cultural similarity ties to board monitoring, we investigate whether the negative relation between cultural similarity and firm value differs among dependent (executive) or independent directors. In this analysis, we construct two new variables. The first variable is the *Cultural Similarity (Independent)* dummy, which equals one if the board consists of a majority of directors that are formally independent, but culturally related to the firm's CEO, and zero otherwise.

The other variable is the *Cultural Similarity-(Dependent)* dummy, which takes a value of one if the board consists of a majority of dependent/executive directors that are both formally and culturally related to the CEO, and zero otherwise.

Focusing on this subsample, we regress *Tobin's Q* on the two new variables and other control variables and report the results in **Table 3.13**. Columns (1) and (2) show that the coefficients on both *Cultural Similarity (Independent)* (*b*=-0.202) and *Cultural Similarity (Dependent)* (*b*=-0.078) are negative and significant at the 1% level. Similarly, Column (3) shows the OLS regression results of Tobin's Q on the two new variables and other control variables. We find that the coefficient on *Cultural Similarity (Independent)* is negative *(b*=-0.178*)* and significant at the 1% level whereas the coefficient on *Cultural Similarity (Dependent)* is negative *(b*=-0.048*)* and significant at 10% level.

This evidence suggests that the CEO-board cultural ties weaken the effectiveness of board monitoring and subsequently reduce shareholder wealth. The negative effect of cultural similarity on firm value is more pronounced in boards with formally independent directors, as cultural ties may prevent conventionally independent directors from performing their monitoring functions.

As for the control variables, we find that the coefficient on *Board Size* is positive and significant, indicating that larger boards achieve higher valuations, which is consistent with prior studies (Pearce and Zahra 1992; Coles et al. 2008; Fauzi and Locke 2012). We also find that the coefficients on *R&D*, *Big4 Auditor* and *Sales Growth*, are respectively positive and significant, indicating that firms with higher R&D, audited by Big 4 auditing firms and with higher growth opportunities are associated with higher firm value, which is in line with Gul et al. (2016).

Table 3. 13: Independent vs. dependent directors

This table exhibits OLS regression estimation results of *Tobin's Q* on board and firm characteristics of Malaysian non-financial listed firms in the sample period of 2009 to 2016. *Tobin's Q* is calculated as market value of assets over book value of assets. *Cultural Similarity (Independent)* and *Cultural Similarity (Dependent)* are the measures of CEO-board cultural similarity computed for dependent and independent directors. All other variables are defined in **Table 3.2**. Standard errors are clustered at the firm level and t-statistics are reported in parentheses. ***, **, * denote statistical significance at the 1%, 5%, and 10% level, respectively.

	Tobin's Q		
	(1)	**(2)**	**(3)**
Cultural Similarity (Independent) (1)	-0.202***		-0.178***
	(-2.869)		(-2.474)
Cultural Similarity (Dependent) (2)		-0.078***	-0.048*
		(-2.813)	(-1.784)
Board Size	0.251***	0.220***	0.246***
	(3.959)	(3.465)	(3.882)
Board Independence	-0.038	-0.093	-0.053
	(-0.295)	(-0.729)	(-0.421)
Board Meeting	-0.062	-0.069*	-0.061
	(-1.631)	(-1.763)	(-1.599)
Firm Size	0.010	0.010	0.008
	(0.708)	(0.711)	(0.581)
Leverage	-0.010	-0.009	-0.009
	(-0.907)	(-0.857)	(-0.866)
R&D	29.095**	31.300**	29.504**
	(2.013)	(2.003)	(2.037)
Sales Growth	0.778***	0.728***	0.763***
	(2.825)	(2.731)	(2.799)
Firm Age	-0.000	0.002	-0.003
	(-0.017)	(0.089)	(-0.108)
Big4 Auditor	0.070**	0.074**	0.070**
	(2.137)	(2.240)	(2.158)
Intercept	-137.927**	-147.914**	-139.713**
	(-2.069)	(-2.054)	(-2.093)
Industry FE	Yes	Yes	Yes
Year FE	Yes	Yes	Yes
Observations	4,400	4,400	4.400
R-squared	0.2504	0.2441	0.2522
H0: (1) = (2) *p*-value			0.0035

3.4.3.3 Controlling for political connections

We further examine whether political connections influence the association between CEO-board cultural similarity and firm value. According to prior studies (Gomez et al. 1999; Gomez 2002; Johnson and Mitton 2003; Abdul Wahab et al. 2015),

Malaysian firms can gain political connections and various favours from government by appointing ethnic Malays as CEOs or directors. Since the introduction of the New Economic Policy in 1970, Malays have been granted priority, financial advantages, and special assistance in various economic policies (Haniffa and Cooke 2002). As a result, they are appointed to the boards in order to gain their personal influence to gain access to capital and various government contracts and sponsored programmes (Mohamad-Yusof et al. 2018). It is as a result of the special privileges they have due to the policy that Malays are appointed to boards. A number of studies have found this to be the case, indicating that firms with a Malay CEO and more Malay directors are more likely to be politically connected (Gul et al. 2016; Mohamad-Yusof et al. 2018).

While political connection assists firms to gain various benefits such as easier access to long-term debt, relaxed taxation and regulatory scrutiny, and stronger market control (Khwaja and Mian 2005; Faccio 2006), it also can jeopardise firm value as a result of the introduction of rent-seeking behaviours (Boubakri et al. 2008). Prior studies have shown inconclusive results on the association between political connection and firm value. For instance, Faccio (2006) documents a positive association between political connection and firm value. Investigating 47 countries, she reveals that political connection is prevalent in countries that are highly corrupt. Similarly, Goldman et al. (2009) show that the announcement of a politically connected individual being nominated to a board leads to positive abnormal stock returns in US firms. However, Fan et al. (2007) find a negative association between politically connected CEOs and post-IPO performance.

Thus, in this section, we examine whether political connections influence the relationship between cultural similarity and firm value and use both Malay CEO and Malay board as proxies for political connection as per prior studies (e.g., Abdul Wahab et al. 2015; Gul et al. 2016). **Table 3.14** shows the results of our OLS regressions after controlling for political connection attributes.

In column (1), we include *Malay CEO* as an additional regressor in our regressions. *Malay CEO* equals one if the firm's CEO is Malay, and zero otherwise. We find the coefficient on *Cultural Similarity* for *Tobin's Q* continues to be significantly negative *(b*=-0.216, *p*<.01*)* after controlling for *Malay CEO*, implying that the main results in **Table 3.5** continue to hold when we control for political connection in our baseline

regressions. Nevertheless, the coefficient on *Malay CEO* is insignificant for *Tobin's Q*, implying that political connection is not associated with firm value.

Next, we further examine whether boards with a majority of Malay directors affect the relationship between cultural similarity and firm value. In column (2), we include *Malay Board* as an additional regressor in our regressions. *Malay Board* equals one if the firm's board has a majority of Malay directors, and zero otherwise. We find the coefficient of *Cultural Similarity* on *Tobin's Q* continues to be significantly negative *(b*=-0.225, *p*<.01) after controlling for *Malay Board*, confirming the validity of our main results after further considering the political connection attribute. Nevertheless, the coefficient on *Malay Board* is insignificant for *Tobin's Q*, implying that political connection is not associated with firm value.

In column (3), we include both *Malay CEO* and *Malay Board* as additional regressors in our regressions. We find that the coefficient on *Cultural Similarity* for *Tobin's Q* continues to be significantly negative *(b*=-0.239, *p*<.01) after controlling for the two proxies for political connection, implying that our main results are unlikely to be driven by the political connection.

As for the control variables, we find that the coefficient on *Board Size* is positive and significant, indicating that larger boards achieve higher valuations, which is consistent with prior studies (Pearce and Zahra 1992; Coles et al. 2008; Fauzi and Locke 2012). We also find that the coefficient on *Board Meeting* is positive and significant, implying that board meeting is associated with higher firm value, whereas the coefficients on *R&D*, *Big4 Auditor* and *Sales Growth*, are respectively positive and significant, indicating that firms with higher R&D, audited by Big 4 auditing firms and with higher growth opportunities are associated with higher firm value, which is in line with Gul et al. (2016). Overall, the results, shown in **Table 3.14**, are qualitatively similar to those reported in **Table 3.5**.

Table 3. 14: Controlling for political connections

This table exhibits OLS regression estimation results of *Tobin's Q* on board and firm characteristics of Malaysian non-financial listed firms in the sample period of 2009 to 2016. *Tobin's Q* is calculated as market values of assets over book value of assets. *Cultural Similarity* is the proportion of board directors that share similar ethnicity with the CEO. *Malay CEO* equals one if the firm's CEO is Malay, and zero otherwise. *Malay Board* equals one if the firm has a majority of Malay directors, and zero otherwise. All other variables are defined in **Table 3.2.** Standard errors are clustered at the firm level and t-statistics are reported in parentheses. ***, **, * denote statistical significance at the 1%, 5%, and 10% level, respectively.

	Tobin's Q		
	(1)	**(2)**	**(3)**
Cultural Similarity	-0.216***	-0.225***	-0.239***
	(-3.110)	(-3.048)	(-3.143)
Malay CEO	-0.008		-0.069
	(-0.175)		(-0.975)
Malay Board		0.016	0.082
		(0.327)	(1.103)
Board Size	0.225***	0.223***	0.222***
	(3.527)	(3.502)	(3.488)
Board Independence	-0.113	-0.123	-0.125
	(-0.882)	(-0.960)	(-0.976)
Board Meeting	-0.068*	-0.073*	-0.072*
	(-1.750)	(-1.857)	(-1.845)
Firm Size	0.009	0.009	0.009
	(0.668)	(0.659)	(0.663)
Leverage	-0.009	-0.009	-0.009
	(-0.855)	(-0.873)	(-0.861)
R&D	29.361**	29.693**	29.602**
	(1.978)	(1.989)	(1.989)
Sales Growth	0.744***	0.740***	0.763***
	(2.825)	(2.798)	(2.847)
Firm Age	-0.002	-0.003	-0.003
	(-0.062)	(-0.098)	(-0.107)
Big4 Auditor	0.073**	0.073**	0.072**
	(2.215)	(2.188)	(2.175)
Constant	-138.945**	-140.436**	-140.105**
	(-2.031)	(-2.041)	(-2.043)
Industry FE	Yes	Yes	Yes
Year FE	Yes	Yes	Yes
Observations	4,389	4,392	4,389
R-squared	0.2489	0.2483	0.2495

3.4.3.4 Cultural diversity and firm value

Although CEO-board cultural similarity has been the main focus in this thesis, we also consider the effect of cultural diversity on the firm value in this section. There is a long-standing theoretical discussion on cultural diversity and how it impacts organisational outcomes. In general, prior studies in corporate governance and management literature indicate cultural diversity as double-edged sword, acknowledging both benefits and costs of cultural diversity (Milliken and Martins 1996; Anderson et al. 2011; Frijns et al. 2016).

On one hand, cultural diversity between individuals stimulates better information flow and effective collaboration, providing a wider range of knowledge, perspectives and skills (Nederveen Pierterse et al. 2013) Due to the great of variety of perspectives, diversity fosters creativity and innovation (Carter et al. 2003). A more diverse board is likely to be more informative and knowledgeable, has healthier information dispensation facilities and can potentially provide benefits particularly in decision makings (Adams et al. 2015). Furthermore, diversity improves board independence and can potentially result in better monitoring effectiveness by the board (Adams and Ferreira 2009; Adams et al. 2015). Thus, cultural diversity may improve firm performance as a result of stronger monitoring role and improved decision makings by the board.

On the other hand, cultural diversity may provide negative impact on firm performance. Prior studies suggest that groups' coordination, collaboration and communication are more confused and less effective in culturally diverse groups (Anderson et al. 2011). Furthermore, cultural diversity can result in lower levels of intragroup trust and understanding, affecting the board members to effectively perform their functions (Frijns et al. 2016), which thereby, could affect firm performance (Erhardt et al. 2003).

In this section, we evaluate the impact of CEO-board cultural diversity on firm value as measured by Tobin's Q. We introduce a new measure of cultural diversity (*Cultural Diversity)*, defined as the proportion of board of directors that has diverse ethnic or cultural background with the CEO.

To evaluate the effect of CEO-board cultural diversity on firm value, we begin the

analysis by regressing *Tobin's Q* on *Cultural Diversity*. **Table 3.15** reports the estimates from our OLS regressions. In column (1), the coefficient on *Cultural Diversity*, as the only explanatory variable, is positive (b=0.106) and significant at the 1% level. Column (2) shows similar results after firm characteristics are introduced (b=0.086, p<.01). Column (3) presents test results after controlling for both board and firm characteristics. The inclusion of the two groups of control variables does not alter the sign or the significance of the *Diversity* (b=*0.087*, p<.01), indicating that the cultural diversity between CEO and board of directors increases firm value.

As for the control variables, we find that the coefficient on *Board Size* is positive and significant, indicating larger boards achieve higher valuations, which is consistent with prior studies (Pearce and Zahra 1992; Coles et al. 2008; Fauzi and Locke 2012). We also find that the coefficient on *Board Meeting* is negative and significant, implying board meeting is associated with lower firm value, whereas the coefficient on *R&D, Big4 Auditor* and *Sales Growth*, are respectively positive and significant, indicating that firms with higher R&D, audited by Big 4 auditing firms and with higher growth opportunities are associated with higher firm value, which is in line with Gul et al. (2016).

Overall, in this section, we show that cultural diversity within CEO-board dyad provide opposite outcomes as compared to CEO-board cultural similarity in our main analyses. The results also consistent with the studies on the positive impacts of board diversity on organisation incomes (Erhardt et al. 2003; Adams and Ferreira 2009; Adams et al. 2015). These studies show that the board diversity is associated with better governance and firm performance.

Table 3. 15: CEO-board cultural diversity and firm value

This table reports the OLS estimation results of *Tobin's Q* on the measure of CEO-board cultural similarity, board characteristics, and firm characteristics for Malaysian non-financial listed firms in the sample period of 2009 to 2016. *Tobin's Q* is calculated as market value of assets over book value of assets. *Cultural Diversity* is the proportion of board directors that has diverse ethnicity with the CEO. All other variables are defined in **Table 3.2**. Standard errors are clustered at the firm level and t-statistics are reported in parentheses. ***, **, * denote statistical significance at the 1%, 5%, and 10% level, respectively.

	Tobin's Q		
	(1)	**(2)**	**(3)**
Cultural Diversity	0.106***	0.086***	0.087***
	(3.544)	(2.844)	(2.949)
Board Size			0.225***
			(3.543)
Board Independence			-0.096
			(-0.753)
Board Meeting			-0.068*
			(-1.746)
Firm Size		0.017	0.010
		(1.196)	(0.708)
Leverage		-0.009	-0.009
		(-0.802)	(-0.825)
R&D		26.766*	30.917**
		(1.800)	(1.998)
Sales Growth		0.651***	0.717***
		(2.678)	(2.723)
Firm Age		0.005	0.001
		(0.187)	(0.039)
Big4 Auditor		0.081**	0.075**
		(2.414)	(2.263)
Intercept	-0.156	-126.557*	-146.185**
	(-1.099)	(-1.846)	(-2.050)
Industry FE	Yes	Yes	Yes
Year FE	Yes	Yes	Yes
Observations	5,157	4,426	4,392
R-squared	0.2034	0.2281	0.2461

3.5 Conclusion

This study has examined the effects of the cultural similarity between CEO and board of directors on firm value as well as the board monitoring effectiveness. The most important findings are highlighted:

First, using OLS regressions, the results from the baseline analysis show a lower Tobin's Q for firms with a higher percentage of cultural similarity between the CEO and other board members. The results remain consistent after controlling for the board and firm characteristics. In terms of economic significance, a one-standard-deviation increase in cultural similarity is associated with a 6.14% decline in firm value. The findings are robust to a variety of robustness tests, including the use of alternative measures of our key variables, alternative estimation methods, and endogeneity concerns.

Second, our additional analyses also suggest that cultural ties are value-relevant and matter and act as a medium of CEO-board relationship, which consequently impairs the effectiveness of board independence. Third, we also find that cultural similarity between the CEO and other board members reduces the frequency of board meetings and, therefore, decreases board vigilance and monitoring. Fourth, this study suggests that cultural ties prevent conventionally independent directors from performing their monitoring functions. Fifth, our main results remain similar after controlling for political connection, as proxied by Malay CEO and board. Finally, we find that CEO-board cultural diversity is associated with increased firm value.

Overall, the results of the analyses from this chapter indicate that cultural similarity can potentially weaken the monitoring effectiveness of board members, and ultimately destroy firm value. Now that we have established that CEO-board cultural similarity reduces firm value as well as the effectiveness of board monitoring and independence, the next chapter will discuss one of the potential causes of the negative evaluation impact of CEO-board cultural similarity. Specifically, the next chapter will examine whether CEO-board cultural similarity influences the quality of financial reporting, as measured by earnings management.

Chapter 4

CEO-Board Cultural Similarity and Earnings Management

4.1 Introduction

Why do firms with a higher fraction of cultural similarity between CEO and directors have lower valuations? In this chapter, we further explore the relationship between CEO-board cultural similarity and the quality of financial reporting to investigate the potential causes of the negative valuation impact of CEO-board cultural similarity.

Recent corporate wrongdoings and scandals such as Enron and WorldCom have caused stakeholders to lose confidence in the credibility of financial reporting, leading to a decrease in shareholder value. As a result, numerous regulators and corporate reforms (e.g., the provisions of Sarbanes Oxley Act 2002) have emphasised numerous shortcomings in the functioning of internal governance mechanisms and attempted to improve them by increasing the responsibilities of the board as well as the CEO in ensuring the integrity of financial reporting. Thus, boards are assumed to discipline the management more effectively and serve as a watchdog for financial reporting quality and process (He et al. 2009; Krishnan et al. 2011). Yet, largely overlooked by these regulations is an analysis of the influence of the CEO's connection with other directors that could impair the board monitoring effectiveness, leading to the reduced financial reporting quality.

Much of the sociology literature also supports the homophily theory, which postulates that 'similarity breeds connection among people' (McPherson et al. 2001). For example, McPherson et al. (2001, p.415) describe that "homophily in race and ethnicity creates the strongest divides in our personal environment", and thus ethnic and racial groups tend to share strong bonds in terms of close friendship. In the corporate board context, we postulate that the similarity in cultural values and backgrounds between managers and directors may serve as an important catalyst

through which social connections and stronger bonds are developed that can enhance trust, empathy, and intimacy between them. These strong bonds would, in turn, affect the effectiveness of board monitoring, especially in curbing managerial opportunism, which could lead to weak internal control over financial reporting.

Several studies find that social ties and a 'friendly board' reduce the board's willingness to monitor and discipline the CEO (Westphal 1999; Adams and Ferreira 2007; Hwang and Kim 2009; Dey and Liu 2010; Nguyen 2012). Another strand of literature has also investigated the relationship between CEO-board social ties and financial reporting quality (e.g., Hoitash 2011; Krishnan et al. 2011; Hwang and Kim 2012; Bruynseels and Cardinaels 2014). However, the findings are equivocal and most of these studies focus on how achieved social ties such as mutual alma mater, employment, and education influence the effectiveness of the board. Limited attention has been given to ascribed social ties through the cultural background, which form an invisible and strong bond that can tie individuals together and establish a basic social network among them. Unlike prior research, this study focuses on the impact of the CEO-board cultural similarity on financial reporting quality. We posit that the CEO-board cultural similarity may jeopardise the board's monitoring task to provide sufficient oversight over the financial reporting quality and process.

To test our hypothesis, we gather a large sample of publicly listed companies in Malaysia and focus on 2009-2016. CEO-board cultural similarity is measured by the fraction of the board of directors that share similar ethnicity with the CEO. Accordingly, we focus on the firm's level of earnings management to measure the quality of reported earnings. We observe earnings management based on signed discretionary accruals because we are more concerned with the board's monitoring role in earnings overstatements which is more prevalent than earnings understatements (Dechow et al. 2012; Hsieh et al. 2014; Zhu et al. 2016). We find that firms with higher CEO-board cultural similarity (henceforth referred to as 'cultural similarity') are more likely to engage in income-increasing accrual-based earnings management. To alleviate the concern over endogeneity that may arise from reverse causality, we use the two-stage least squares (2SLS) instrumental variables approach and find consistent results. In further robustness analysis, we use real earnings management as an alternative earnings management proxy. We find that firms with higher cultural

similarity are more likely to engage in real-activities earnings management through overproduction activities than sales and discretionary expenses activities.

We then explore the extent to which the propensity of firms with higher cultural similarity to manage earnings is driven by the presence of powerful CEOs. Prior studies suggest that entrenched CEOs can abuse their power to manipulate earnings numbers to maintain their position or increase their compensation (Healy and Wahlen 1999). Using CEO duality as a proxy for CEO power, we do not find evidence that CEO power affects the relationship between cultural similarity and earnings management.

Traditionally, a director is identified as independent if s/he has neither financial nor familial connections to the CEO. However, prior research has shown that social ties can also be a potential source of a director's dependence on the CEO (Hwang and Kim 2009; Hoitash 2011; Fracassi and Tate 2012). Motivated by the existing studies, we also argue that cultural ties between the CEO and other board members can affect the effectiveness of board independence. To test this proposition, we develop a new definition of board independence, which takes into account both the formal definition of director independence and the cultural ties between the CEO and other board members. We find that our newly proposed independence measure is more negatively related to earnings management than boards that are only conventionally independent, implying that boards are more effective at controlling agency issues and limiting managerial opportunism when they are both conventionally and culturally independent from the CEO.

We also find that the positive effect of CEO-board cultural similarity on income-increasing accrual-based earnings management is more prevalent among independent directors, indicating that cultural similarity impairs the ability of independent directors to mitigate managerial opportunism and earnings manipulation. We further document a negative association between CEO-independent directors' cultural similarity and the abnormal levels of discretionary accruals, implying that the similarity does not affect the ability of independent directors to monitor the CEOs to stop them engaging in the real earnings management. Meanwhile, we find no evidence that cultural similarity between CEO and dependent directors affects either accrual-based or real earnings management. Overall, our evidence suggests that cultural similarity is more likely to

disrupt the monitoring tasks of independent directors than those of dependent directors.

Finally, we redefine our variable of interest as the fraction of audit-committee members that share a similar culture to the CEO and find no evidence that the CEO-audit committee affects earnings management. This implies that CEO-board cultural similarity is more powerful than CEO-audit committee cultural similarity in explaining the variation in earnings management. Taken collectively, our results highlight the importance of analysing the CEO's cultural ties with the board as a whole rather than just with the audit committee. As suggested by prior research (DeFond et al. 2005; Krishnan and Visvanathan 2007; Krishnan et al. 2011), the audit committee's effectiveness may be contingent on the corporate governance the firm has in place, and its effectiveness may be weakened in practice by a dysfunctional board.

Overall, our results indicate that CEO-board cultural similarity leads to weak internal control over financial reporting, which could be one of the potential sources of the negative valuation impact of cultural similarity that was evident in the previous chapter. Our contribution to the literature is threefold. First, while much research highlights the relevance of the country-level cultural distance to foreign investments, there is relatively little empirical work on the potential effect of cultural similarity between managers and other board members on corporate decisions. We fill this void by providing the first empirical evidence on the impact of the CEO-board cultural ties on the effectiveness of board monitoring. We complement recent studies on the governance relevance of culture (e.g., Li and Harrison 2008a, 2008b; Bryan et al. 2015; Frijns et al. 2016; Nguyen et al. 2018) by focusing on how the CEO-board cultural similarity affects the effectiveness of board monitoring and the propensity to manipulate earnings. Our study also complements the nascent literature on the role of culture in business, financial decision-making, and organisational outcomes[10]. We contribute to this stream of research by highlighting the relevance of the CEO-board cultural similarity to the practice of earnings management.

Second, we contribute to the growing research on how the CEO-board relationship can shape corporate outcomes. Prior studies focus mainly on the social reciprocity

[10] Among these studies are Ahern et al. (2015), Boubakri and Saffar (2016), El Ghoul and Zheng (2016), Holderness (2017), Li et al. (2013), Lievenvruck and Schmid (2014), Shao et al. (2010), Shao et al. (2013), Siegel et al. (2011) and Zheng et al. (2012).

between CEO and other directors, showing that such reciprocity weakens board monitoring intensity and reduces firm value (e.g., Hwang and Kim 2009; Fracassi and Tate 2012; Lee et al. 2014; Goergen et al. 2015). We complement this literature by documenting that the common cultural values between the CEO and other board members impair both the monitoring effectiveness of the board and financial reporting quality. Finally, we add to the extant literature on executives' incentives to manage earnings by identifying CEO-board cultural ties as a new determinant of the propensity to manipulate earnings (Bergstresser and Philippon 2006; Krishnan et al. 2011).

The rest of this chapter is organised as follows. **Section 4.2** provides a brief review of the related literature and develops our hypothesis. **Section 4.3** discusses our methods and data. **Section 4.4** reports our results and **Section 4.5** concludes.

4.2 Literature review and hypothesis development

4.2.1 Earnings management

Due to the importance of earnings information to the users of financial statements, especially investors and other stakeholders in decision-making, the exercise of earnings management has been critically debated for many years. Although definitions of earnings management are rife, accounting academics mainly depend on Healy and Wahlen's (1999) definition, which states that earnings management occurs *"…when managers use judgment in financial reporting and in structuring transactions to alter financial reports to either mislead some stakeholders about the underlying economic performance of the company or to influence contractual outcomes that depend on reported accounting practices...*" (Healy and Wahlen 1999, p.368).

Despite its potential adverse effect on the informativeness and reliability of earnings, earnings management has been allowed under the generally accepted accounting principles (GAAP). Numerous studies have attempted to explain firms' motives for earnings management. In general, firms tend to exercise earnings management for opportunistic purposes, such as the avoidance of earnings losses and decreases (Burgstahler and Dichev 1997), meeting analysts' earnings forecasts (DeGeorge et al.

1999), or around important corporate events (e.g., Teoh et al. 1998a, 1998b; Shivakumar 2000; Ducharme et al. 2004; Cohen and Zarowin 2010).

In addition to the literature on the firms' propensity to manage earnings, several studies also investigate the managerial incentives for earnings management. For instance, Healy (1985) shows that managers manipulate earnings in response to their bonus schemes. Bergstresser and Philippon (2006) also find that CEOs are prone to engage in earnings management when their total compensation is more closely tied to the value of stock and option holdings. Similarly, Burns and Kedia (2006) document higher earnings management when CEOs hold large option portfolios in their firms. In a slightly different context, Leuz et al. (2003) document widespread earnings management practice in countries with weaker investor protection. We contribute to this strand of research by investigating the extent to which the CEO-board cultural similarity spurs managers to manipulate earnings.

Although managers have several tools at their disposal to manipulate earnings,[11] the accrual-based and real activities management are particularly popular in practice (Healy and Wahlen 1999; Roychowdhury 2006; Cohen and Zarowin 2010; Kothari et al. 2016). While accrual-based earnings management involves the management choice from a set of generally accepted accounting policies to accomplish their earnings targets, real-earnings management is practised by undertaking actions that change the timing or structuring of operations and/or diverge from normal business activities (Roychowdhury 2006). Compared to accrual-based earnings management, real earnings management is deemed to be more expensive, has a direct effect on the cash flows (Graham et al. 2005, Kim and Sohn 2013), and is more likely to destroy the firm value (Gunny 2010). However, despite its adverse effect on firm value, some firms may still opt for real earnings management to avoid market discipline. Consistent with this view, several studies show that real earnings management receives relatively less scrutiny by media, public, regulators, and auditors than accrual-based earnings management (Kim and Sohn 2013; Francis et al. 2015). In addition, real earnings management can be practised throughout the year, whereas accrual-based earnings management is, generally, limited to certain periods (Zang 2012). Overall, managers tend to favour the trade-off between the costs and benefits of the accrual and real

[11] This includes changing the accounting choice, manipulating total accruals/discretionary accruals, managing real activities/transaction, and changing the distribution of earnings or smoothing income.

earnings management and select a strategy that suits their incentives (Cohen et al. 2008; Cohen and Zarowin 2010; Zang 2012).

To mitigate opportunistic earnings management activities, government regulations often restrict managers' ability to manipulate reported accounting numbers to the public. For instance, the Sarbanes-Oxley Act was introduced by the US authorities to curb corporate fraud following the emergence of corporate scandals and headline-producing ethical failures, such as Enron's notorious scandals in 2001. Corporate governance codes, such as those relating to the monitoring role of board directors and audit committees, may also constrain managers' unethical practice of earnings management. However, whether the board of directors can effectively curb managers from manipulating earnings remains questionable as its oversight role could be jeopardised by factors that may affect its independence. Despite the ample research on the determinants of board independence (Adams 2003, Adams and Ferreira 2007; Chen et al. 2015; Stein and Zhao 2019), little has been done to relate culture to the board's effectiveness in enhancing financial reporting quality. In this study, we are interested in investigating the impact of the management-board's cultural similarity on managers' propensity to manipulate earnings.

4.2.2 Board monitoring and earnings management

Separation of ownership and control has become the key principle of a concrete governance system in the modern business world. Several studies investigate the role of the board of directors and its effectiveness in monitoring and controlling management from earnings management practice (e.g., Hermalin and Weisbach 2003; Klein 2002; Xie et al. 2003; Park and Shin 2004; Peasnell et al. 2005). These studies have concurred that board independence is the vital criterion for a concrete governance system to uphold financial reporting credibility. Following some highly publicised financial reporting failures, such as Enron and WorldCom, new rules and regulations have been introduced to strengthen the internal governance mechanisms, such as board composition and independence. For example, in the US, the NYSE, and NASDAQ in 2002 as well as the Sarbanes Oxley Act 2002 have emphasised that listed firms must have a majority of independent directors on their board. As a result, some studies have directly examined the effects of the increased board independence due to the corporate governance reforms on financial reporting quality and earnings management (Bédard

et al. 2004; Chen et al. 2015). For instance, Chen et al. (2015) finds that the increases in board independence are effective in reducing earnings management, especially when the independent directors have easier access to information. Overall, the studies presented thus far provide evidence that board independence is a critical feature in protecting the credibility of the financial reporting process, particularly in terms of deterring managers from earnings management practice.

Nevertheless, it is possible to argue that the effectiveness of board independence could be jeopardised by the informal connections between management and the board. Although directors may be independent according to regulations such as SOX or other listing requirements, they may still be informally connected to the CEO; in turn, such connections may reduce the effectiveness of boards in monitoring managers. For example, Langevoort (2007) documents that social friendship (i.e., membership in the same club, associations, or charitable organisations) between the board and managers can weaken the shareholder primacy. Hwang and Kim (2009) also find that socially connected boards award higher CEO compensation. Similarly, Dey and Liu (2010) suggest that the social ties between CEO and board weaken the monitoring effectiveness of the board. However, only a few studies examine the role of the informal connections between CEOs and other board members in the context of financial reporting quality. One such study is that by Krishnan et al. (2011), who examine the extent to which social ties between CEO and board arising from current or prior employment, education, and other activities (such as golf clubs or charity organisation) influence earnings management. Meanwhile, Hwang and Kim (2012) exhibit that CEO-audit committee social ties enable the exercise of creative accounting. Overall, both studies indicate that such social ties weaken the financial reporting system and lower the information quality. We extend and complement this line of research by investigating whether culture, as one of the important determinants of the close relationship between CEO and board, affects the board monitoring effectiveness and financial reporting process.

4.2.3 Hypothesis development

Drawing from homophily theory and social identity theory, we elucidate that cultural similarity may motivate individuals to identify themselves into the same group and that similarity in cultural background and values could also catalyse and facilitate

relationships among individuals (Tajfel and Turner 1986; McPherson et al. 2001). In the corporate board context, we postulate that the similarity in cultural values and backgrounds between managers and directors may serve as an important catalyst through which social connections and stronger bonds are developed. These strong bonds would, in turn, affect the effectiveness of board monitoring, especially in curbing managerial opportunism, which could lead to weak internal control.

Specifically, we hypothesise that cultural similarity between the CEO and other board members reduces board monitoring effectiveness and ultimately financial information quality. The shared cultural values and background enhance trust, empathy, and intimacy between the two parties.[12] This should lead to less scrutinising and critical judgment of the actions and decisions proposed by the CEOs, constraining the board to perform the intended roles of an unbiased monitor.

Furthermore, numerous studies have shown that social ties as well as 'friendly boards' lower the monitoring effectiveness of the board (Westphal 1999; Adam and Ferreira 2007; Hwang and Kim 2009; Dey and Liu 2010). Specifically, these studies indicate that the social ties between the two parties are negatively related to the board's willingness to monitor and discipline the CEO. Another extant strand of literature has also examined the relationship between CEO-board social ties and financial reporting quality (e.g., Krishnan et al. 2011; Hoitash 2011; Hwang and Kim 2012; Bruynseels and Cardinaels 2014). However, the findings are inconclusive and most of these studies have focused on the relevance of achieved social ties such as mutual alma mater, employment, and education in influencing the effectiveness of the board. However, little attention has been paid to ascribed social ties through the cultural background, which form an invisible and stronger bond that can tie individuals together and establish a basic social network among them. Unlike prior research, we argue that the presence of cultural similarity between the board and CEOs may jeopardise the board's monitoring role in ensuring fair and unbiased reporting. The reduced monitoring may, in turn, spur CEOs to act and make decisions in their own interests; for example, engage in earnings management practice to smooth earnings.

[12] As according to McPherson et al. (2001), the social ties based on ethnicity and race, which are commonly embedded with culture, are more likely to create strong bonds between individuals.

Moreover, prior research has shown that managers are more likely to engage in income-increasing, rather than income-decreasing, earnings management, to achieve earnings objectives (Dechow et al. 2012; Hsieh et al. 2014; Zhu et al. 2016). Consistent with this notion, CEOs with higher cultural connections with other board members might abuse the connection by engaging in income-increasing earnings management to accomplish earnings targets. Hence, we argue that the CEO-board cultural similarity has a positive impact on income-increasing earnings and hypothesise that:

Hypothesis: *There is a positive relation between CEO-board cultural similarity and income-increasing earnings management.*

4.3 Data, variables measurements, and descriptive statistics

4.3.1 Data and sample selections

To investigate the impact of CEO-board cultural similarity on earnings management, we obtain our initial sample which comprises all non-financial firms listed on the main market of Bursa Malaysia (previously known as Kuala Lumpur Stock Exchange) over the period from 2009 to 2016. We collect financial and accounting data from the Worldscope (DataStream) as well as S&P Capital IQ database to compute accrual-based earnings management and real activities management measures. Non-financial information and corporate governance data such as CEO and board characteristics were manually collected from annual reports, which were retrieved from www.bursamalaysia.com as well as Bloomberg. Following the prior research on earnings management, we exclude firms in the financial services (SIC 6000-6999) and utilities industries (SIC 4900-4999) due to their special regulatory environment, corporate governance practices and accrual procedures (Kuang et al. 2014; Cheng et al. 2016). Our sample starts from 2009, as it represents the stable period of Malaysia's financial and economic conditions after the global financial crisis that occurred during 2007-2008. We also eliminate firm-year observations with missing or incomplete financial data for calculating earnings management measures. To mitigate the impact of extreme values and the outliers problem, we winsorise each of the continuous variables used in the regressions at the top and bottom 1%. For our main test, the final

sample consists of 3,588 firm-year observations from 621 firms over the sample period. The detailed sample selection process is shown in **Table 4.1**.

Table 4. 1: Sample selection process

This table reports the sample selection process and resulting firm-year observations. We begin with all listed firms on Capital IQ from 2009 to 2016. After deleting observations in financial and regulated industries as well as observations with incomplete financial and governance data, we have 3,588 from 2009 to 2016.

No		Number of observations
1	Total number of firm-year observations from 2009 to 2016	7,448
2	Observations in financial (SIC 6000-6999) and utilities industries (SIC 4900-4999)	(1,327)
3	Observations with incomplete data (financial or corporate governance)	(2,533)
	Final Sample	3,588
	No of unique firms	621

4.3.2 Variables definition

4.3.2.1 Measuring cultural similarity

The measurement of cultural similarity and the construction of our key variable of interest, the cultural similarity between CEO and other board directors (*Cultural Similarity*), were previously discussed in more detail in **Section 2.4.4.**

4.3.2.2 Measuring earnings management

To examine earnings management, we first study a firm's discretionary accruals in our main analysis. Following prior research (Kuang et al. 2014; He 2016), we estimate the discretionary accruals with the cross-sectional form of the modified Jones model (Dechow et al. 1995; Dechow et al. 2012).

$$\frac{TA_{i,t}}{A_{i,t-1}} = \beta_1 \frac{1}{A_{i,t-1}} + \beta_2 \frac{\Delta REV_{i,t} - \Delta REC_{i,t}}{A_{i,t-1}} + \beta_3 \frac{PPE_{i,t}}{A_{i,t-1}} + \varepsilon_{i,t} \qquad (\mathbf{4.1})$$

where for each firm *i*, $TA_{i,t}$ is the total accounting accruals at the end of year *t*, estimated as earnings before extraordinary items minus net cash flows from operations; $A_{i,t-1}$is total assets at the end of year *t-1*; $\Delta REV_{i,t}$ is the change in sales revenue between year *t* and year *t-1*; $\Delta REC_{i,t}$is the change in accounts receivable

between year *t* and year *t-1*; $PPE_{i,t}$ is property, plant, and equipment at the end of year *t*; and $\varepsilon_{i,t}$ is an error term. We run the cross-sectional OLS regression in Eq. (**4.1**) for each SIC industry-year with at least 15 observations. This approach is widely used in order to control for any industry-wide change in economic condition that could affect accruals (Defond and Jiambalvo 1994: Kaznik 1999).

Next, we use the estimated coefficient from Eq. (**4.1**) to compute the discretionary accruals as follows:

$$DACC_{i,t} = \frac{TA_{i,t}}{A_{i,t-1}} - [\beta_1 \frac{1}{A_{i,t-1}} + \beta_2 \frac{\Delta REV_{i,t} - \Delta REC_{i,t}}{A_{i,t-1}} + \beta_3 \frac{PPE_{i,t}}{A_{i,t-1}}] + \varepsilon_{i,t} \qquad (\mathbf{4.2})$$

where $DACC_{i,t}$ is the estimated discretionary part of total accruals for firm *i* at time *t* and $DACC_{i,t}$ is the discretionary accruals, defined as total accruals minus the fitted normal accruals.

The dependent variable is the signed value of discretionary accruals (S*DA*) of each firm year and the variable of interest is *Cultural Similarity*. We observe earnings management based on signed discretionary accrual because we are more concerned with the board's monitoring role in earnings overstatements which is more prevalent than earnings understatements (Dechow et al. 2012; Hsieh et al. 2014; Zhu et al. 2016).

4.3.2.3 Control variables

Following prior literature, we include several control variables in our baseline regressions. First, we control for return on assets (*ROA*), a proxy for firm performance, as firm performance may influence manager's incentive to engage in earnings management (Chung et al. 2002). Firms with poor performance are likely to engage more in earnings management. Furthermore, we also include the market-to-book ratio (*Market-to-Book*), as a proxy for a firm's growth opportunities. Prior literature on earnings management shows that firms with higher market-to-book ratios are more likely to practise earnings management (Cheng and Warfield 2005; Zang 2012). Existing literature also suggests that larger firms are more likely to engage in earnings management (DeFond and Park 1997; Chung et al. 2002). Thus, we include firm size (*Firm Size*), measured by the natural logarithm of the firm's total assets, as one of the control variables.

We also include financial leverage (*Leverage*), since firms with higher leverage may be under pressure to maintain earnings levels (Klein 2002; Peasnell et al. 2005; Franz et al. 2014). In addition, we control for return volatility (*Return Volatility*), as some firms are likely to manage volatile performance (Hribar and Nichols 2007). As firms that are audited by one of the Big 4 auditing firms tend to report lower levels of discretionary accruals (Becker et al. 1998; Francis et al. 2015), we also include a dummy variable (*Big4 Auditor*), which takes the value of one if the company is audited by one of the big auditors, in our regression. In addition, we include *Sales Growth*, the one-year percent change in sales from year $t-1$ to year t to account for actual sales growth, and *Firm Age*, the natural logarithm of the number of years since a firm was established.

Prior literature suggests that effective corporate governance constrains earnings management (e.g., Xie et al. 2003; Peasnell et al. 2005; Chiu et al. 2013). We account for such an effect by including i) *Board Independence* (the percentage of independent directors), ii) *Board Meeting* (the natural logarithm of the number of annual boards of director meeting), and iii) *Board Size* (the natural logarithm of the number of directors on the board) as additional controls in our regressions. Detailed variable definitions can be found in **Table 4.2**.

Table 4. 2: Variable definitions and data sources

Variable	Definition	Sources
Dependent variables		
SDA	Signed discretionary accruals, from Modified Jones (Dechow et al. 1995) model.	Capital IQ
AB_CFO	Abnormal level of operating cash flows, the measure of sales manipulation.	Capital IQ
AB_PROD	Abnormal level of production costs, the measure of overproduction.	Capital IQ
AB_DIS	Abnormal level of discretionary expenses, the measure of discretionary expenditure reduction.	Capital IQ
RM1	The aggregate measure of abnormal level of production costs and discretionary expenses.	Capital IQ
RM2	The aggregate measure of abnormal level of operating cash flows and discretionary expenses.	Capital IQ
RM3	Aggregate measures of real earnings management.	Capital IQ
Independent variables		
Cultural Similarity	The proportion of board directors that share similar culture/ethnicity with the CEO. i.e., the number of directors that share a similar ethnic background with the CEO/total number of directors.	Bloomberg and annual report
Board characteristics		
Board Size	The number of directors on the board; log-transformed	Annual report
Board Meeting	The number of annual boards of directors' meetings; log-transformed.	Annual report
Board Independence	The percentage of independent directors on board.	Annual report
Firm characteristics		
Firm Size	The natural logarithm of total assets.	Capital IQ
Firm Age	The number of years since the firm's founding; log-transformed.	Capital IQ and annual report
Firm Leverage	Total debt to assets (total debts divided by total asset); log-transformed.	Capital IQ
Return Volatility	The standard deviation of monthly stock returns during a calendar year (in %).	DataStream
Big 4 Auditors	An indicator variable with the value of 1 if audited by Big 4 auditors, and 0 otherwise	Annual report
Sales Growth	The annual growth rate of the firm's total assets; scaled and log-transformed	Capital IQ
Market-to-Book Ratio	(market price of share) divided by (shareholders' equity divided by the number of ordinary shares outstanding)	Capital IQ
ROA	Operating income divided by the year-end book value of total assets; scaled and log transformed	Capital IQ

4.3.3 Descriptive statistics and correlation matrix

Table 4.3 presents the descriptive statistics of the variables used in our analysis. The average *Cultural Similarity* is 0.69, suggesting that the majority of the directors on the board share similar culture/ethnicity with the company's CEO. The average *Board Size* is about 7 members and ranges from 3 to 22 members. In terms of *Board Independence*, the mean of independent members on the board is 47%, with values ranging from 11% to 100%. The average frequency of *board meetings* in a year is 5 times and ranges from 0 to 27 times per year.

For firm characteristic variables, the average size of firms is 2053.47 million MYR and the average firm age is 28.75 years. Average *Sales Growth* is around 12% and the *Leverage* ratio has a mean value of 0.18. The average firm age is 28.75 years. In addition, the big four auditor dummy (*Big4 Auditor*) has a mean value of 0.45, implying that only 45% of the sample companies are audited by one of the Big 4. The large variation in the *ROA* indicates that Malaysian companies differ greatly in their profitability. These statistics differ slightly from those of Gul et al. (2016) and Bhatt and Bhatt (2017), presumably as our sample contains more recently listed firms. On average, the monthly return volatility is 11.65%, consistent with previous research conducted on Malaysian firms (Gul et al. 2016).

Furthermore, the mean value of *SDA* is 0.01, revealing that the magnitude of signed discretionary accruals is about 1.1%, which is consistent with Hsieh et al. (2014). Furthermore, the mean value of real earnings management measures, (*AB_CFO, AB_PROD, AB_DIS, REM1, REM2, REM3*) are all 0.01, which is also in line with previous research (Hsieh et al. 2014)

Table 4.4 reports the Pearson correlation coefficients for the regression variables. Most of the pairwise correlations among the independent variables are below 0.50, indicating that collinearity is unlikely to be a major problem in our analyses. We also compute the variance inflation factor (VIF) for all independent variables. The largest one is 2.35, far below a recommended threshold value of 10.00 for multiple regression models (Hair et al. 1998; Kennedy 1998), confirming that multicollinearity is not a serious problem in our study.

Table 4. 3: Summary statistics

This table reports summary statistics for CEO-board cultural similarity, earnings management measures and control variables for a sample containing the non-financial firms listed in Bursa Malaysia. The final sample contains unbalanced panel data for 620 Malaysian firms for the period between 2009 and 2016. All variables are as defined in **Table 4.2**.

Variable	Obs.	Mean	Stdev.	Min.	0.25	Median	0.75	Max.
Cultural Similarity	5670	0.69	0.23	0.00	0.57	0.75	0.83	1.00
Board Size	5,641	7.33	1.94	3.00	6.00	7.00	8.00	22.00
Board Independence	5,643	0.47	0.13	0.11	0.38	0.44	0.57	1.00
Board Meeting	5,637	5.40	1.97	0.00	4.00	5.00	6.00	27.00
Firm Size	6,008	2053.47	1323.94	1.00	868	2060.5	3237.5	4308
Leverage	5,694	0.18	0.23	0.00	0.03	0.15	0.29	10.9
Sales Growth	5,590	0.12	1.46	-62.9	-0.09	0.04	0.17	49.58
Firm Age	6,049	28.75	20.56	1.00	25.00	25.00	37.00	188
Big4 Auditor	5,701	0.46	0.46	0.00	0.00	0.00	1.00	1.00
ROA	5,685	0.05	0.11	-0.88	0.01	0.05	0.10	0.96
Market-to-Book	5688	0.00	0.01	-0.62	0.00	0.00	0.00	0.16
Return Volatility	5398	11.26	8.63	1.34	5.97	9.11	13.73	93.07
SDA	4554	-0.01	0.18	-2.44	-0.05	-0.01	0.05	5.57
AB_CFO	5502	-0.01	0.13	-2.31	-0.05	-0.01	0.05	2.42
AB_PROD	5502	-0.01	0.17	-2.36	-0.07	0.01	0.08	2.96
AB_DIS	5502	0.01	0.11	-0.65	-0.05	-0.01	0.04	1.43
RM1	5502	-0.01	0.15	-2.22	-0.06	0.01	0.07	2.88
RM2	5502	-0.01	0.17	-1.38	-0.08	-0.01	0.07	2.80
RM3	5502	-0.01	0.30	-2.78	-0.12	0.02	0.15	3.17
Board Ind-new	5734	0.13	0.19	-0.80	0.00	0.10	0.24	1.00
Independent	5734	0.33	0.20	0.00	0.20	0.33	0.44	1.00
Dependent	5734	0.17	0.43	-0.82	-0.20	0.00	0.60	1.00

Table 4. 4: Correlation matrix

This table reports the correlation matrix among the main variables used in our econometric analyses. Correlation coefficients significant at the 1% level or better are in bold. Refer to **Table 4.2** for the description of a detailed variable.

	Variables	**1**	**2**	**3**	**4**	**5**	**6**	**7**	**8**	**9**	**10**	**11**	**12**	**13**
1	*Cultural Similarity*	1												
2	*Board Size*	--0.012	1											
3	*Board Independence*	**-0.007**	**-0.371**	1										
4	*Board Meeting*	**-0.049**	**0.133**	**0.088**	1									
5	*Firm Size*	**-0.049**	**0.250**	0.004	**0.289**	1								
6	*Leverage*	-0.027	**0.088**	-0.012	**0.065**	**0.185**	1							
7	*Sales Growth*	-0.005	-0.004	0.015	0.005	-0.002	0.004	1						
8	*Firm Age*	**-0.130**	**0.093**	0.016	**0.033**	**0.167**	0.012	**-0.035**	1					
9	*Big4 Auditor*	**-0.072**	**0.180**	**-0.095**	**0.086**	**0.189**	**0.062**	-0.009	**0.189**	1				
10	*ROA*	-0.001	**0.113**	**-0.092**	**-0.083**	0.024	**-0.066**	**0.036**	**0.074**	**0.109**	1			
11	*Market-to-Book Ratio*	**-0.041**	**0.053**	**-0.033**	0.026	**0.077**	**0.050**	-0.000	-0.013	**0.055**	**0.108**	1		
12	*Return Volatility*	0.008	**-0.105**	**0.057**	0.009	**-0.076**	0.002	0.013	**-0.108**	**-0.128** -	**-0.082**	-0.024	1	
13	*SDA*	0.024	-0.009	**0.029**	**-0.039**	0.006	**-0.043**	0.026	0.005	-0.00	**0.115**	**-0.029**	**0.091**	1

4.4 Empirical results

To estimate the impact of cultural similarity between CEO and directors on earnings management, we estimate the following regression for firm *i* in year *t:*

$$SDA = a_0 + a_1 Cultural\ Similarity_{it} + a_2 Board\_Characteristics_{it} + a_3 Firm\_Characteristics_{it} + Industy\ dummies + Year\ dummies + \varepsilon_{it} \quad \textbf{(4.3)}$$

where earnings management is measured by *SDA*, which represents signed discretionary accruals; *Cultural similarity* is measured by the proportion of board directors that share similar ethnicity with the CEO; board characteristics are a set of variables that comprise *Board Independence*, *Board Size*, and *Board Meeting*; firm characteristics variables comprise *Leverage*, *Firm Size*, *Firm Age*, *Sales Growth*, *Market-to-Book Ratio*, *ROA*, *Return Volatility*, and *Big4 Auditor*; two-digit SIC *industry dummies* are included to account for the industry fixed effect and *Year dummies* are added to account for the time effect. All the variables are as previously defined. Standard errors are clustered at the firm level for all regressions.

4.4.1 CEO-board cultural similarity and accrual-based earnings management

In this section, we investigate the relation between CEO-board cultural similarity and earnings management. The variable of interest is the CEO-board cultural similarity, *Cultural Similarity*, which is the proportion of board directors that share similar ethnicity with the CEO and signed discretionary accrual (*SDA*) of each firm-year is our dependent variable.

Table 4.5 presents the OLS estimations results of the signed discretionary accruals on CEO-board cultural similarity, *Cultural Similarity*. Column (1) reports the results when *Cultural Similarity* is included as the only explanatory variable. The coefficient on *Cultural Similarity* is positive but insignificant.

In column (2), we control for firm characteristics, namely *Leverage*, *Firm Age*, *Firm Size*, *Sales Growth*, *Market-to-Book ratio*, *ROA*, *Return Volatility*, and *Big4 Auditor*. We find that the coefficient on *Cultural Similarity* is positive and statistically significant at the 10% level (b=0.026, t=1.882). The coefficients on the control variables, such as *Market-to-Book Ratio* and *ROA*, are consistent with those in previous studies. The findings suggest that firms are likely to engage in income-

increasing earnings management (accrual-based) when they have a lower market-to-book ratio, which is consistent with Kuang et al. (2014). Similar to Rangan (1998), we also find that firms with better performance, as proxied by higher ROA, are more likely to engage in income-increasing earnings management.

Next, in column (3), we further control for a set of board characteristics, *Board Independence*, *Board Meeting*, and *Board Size*. The results suggest that the estimated coefficient on *Cultural Similarity* remains positive and significant at the 5% level (b=0.031, t=2.242) after controlling for board characteristics, indicating that CEO-board cultural similarity is associated with higher engagement in income-increasing earnings management (accrual-based).

As for the control variables, we find that the coefficient on *Board Independence* is positive and statistically significant at the 1% level, implying that firms engage more in income-increasing earnings management when there is a higher percentage of board independence, and further implying a positive relationship between board independence and income-increasing earnings management.[13] We also find that the coefficient on *Board Meeting* is negative and statistically significant at the 5% level, implying that firms engage less in income-increasing earnings management when there is a higher frequency of board meetings, which is consistent with Xie et al. (2003).

Overall, our results in **Table 4.5** support our **hypothesis**, implying that firms with a higher fraction of CEO-board cultural similarity are more likely to engage in income-increasing earnings management (accrual-based).

[13] Most of the prior research finds a negative relationship between board independence and earnings management (Klein 2002; Cornett et al. 2009). However, results of board independence on corporate misconduct such as earnings management are mixed (Neville et al. 2019). There are also studies that report board independence is insignificantly associated with earnings management (Chen et al. 2015). Several studies even find a positive relationship between board independence and financial restatements (Arthaud-day et al. 2006; Gomulya and Boeker 2014).

Table 4. 5: CEO-board cultural similarity and accrual-based earnings management

This table reports the OLS estimation results of accrual-based earnings management on a measure of CEO-board cultural similarity, board characteristics, and firm characteristics for Malaysian non-financial listed firms in the sample period of 2009 to 2016. Accrual-based earnings management is measured as *Signed Discretionary Accruals (SDA)*. *Cultural Similarity* is the proportion of board directors that share similar ethnicity with the CEO. All other variables are defined in **Table 4.2**. Standard errors are clustered at the firm level and t-statistics are reported in parentheses. ***, **, * indicate statistical significance at the 1%, 5%, and 10% level, respectively.

	Signed Discretionary Accrual (SDA)		
	(1)	**(2)**	**(3)**
Cultural Similarity	0.017	0.026*	0.031**
	(1.370)	(1.882)	(2.242)
Board Independence			0.082***
			(3.030)
Board Meeting			-0.023**
			(-1.997)
Board Size			0.004
			(0.302)
Leverage		0.014	0.016
		(0.418)	(0.468)
Firm Age		-0.000	-0.000
		(-0.131)	(-0.359)
Firm Size		0.002	0.003
		(0.736)	(1.174)
Sales Growth		0.000	0.000
		(0.908)	(0.650)
Market-to-Book Ratio		-0.000***	-0.000**
		(-2.595)	(-2.557)
ROA		0.195***	0.233***
		(5.303)	(5.910)
Return Volatility		0.000	0.000
		(0.453)	(0.545)
Big4 Auditor		-0.006	-0.005
		(-0.798)	(-0.712)
Intercept	-0.014	-0.033	-0.060
	(-1.550)	(-1.073)	(-1.312)
Industry FE	Yes	Yes	Yes
Year FE	Yes	Yes	Yes
Observations	3,841	3,612	3,588
R-squared	0.0005	0.0185	0.0240

4.4.2 Robustness analyses

This section conducts a series of robustness tests to ensure that the findings in **Table 4.5** are robust, including an endogeneity test by using the instrumental variable

approach and alternative measures of earnings management, i.e., real earnings management.

4.4.2.1 Endogeneity test using the instrumental variable approach

Our baseline regression result shows a positive relation between CEO-board cultural similarity and income-increasing accrual-based earnings management. However, the results might be subject to endogeneity concerns. For instance, a firm's decision to appoint a CEO who has a similar cultural background to other directors on the board may not be random, causing a potential self-selection bias. In addition, it is plausible that some omitted variables which affect both the appointment of a CEO that shares a similar cultural background with other board members and accrual-based earnings management may drive our results. Furthermore, there is a reverse causality concern that firms with higher earnings quality may also be more responsive to calls for lower CEO-board cultural similarity, or vice versa. This would suggest that CEO-board cultural similarity in our study could be endogenous.

To alleviate these endogeneity concerns, we use the two-stage least squares (2SLS) instrumental variable approach. Particularly, we employ an instrument that is unlikely to exert an effect on accrual-based earnings management but should have an indirect relationship through its effects on CEO-board cultural similarity. The instrument we use in our study is a dummy variable for whether a firm is headquartered outside of a large metropolitan city. One of the motivations deciding this instrument is that we expect firms headquartered in the small towns or outside of a large metropolitan area to be less culturally diverse than firms headquartered in larger city. This argument is consistent with Frijns et al. (2016) and Masulis et al. (2012) concerning their instruments which are mainly focused on the location of firms' headquarters as their instruments of board heterogeneity or cultural diversity.

We report the first-stage regression results in column (1) of **Table 4.6,** where we regress cultural similarity on our instrument, together with the controls used in the second-stage regression. The significantly positive association between the instrumental variable and *Cultural Similarity* suggests that our instrument is valid.

To assess the strength of our instrumental variables, we perform a standard test for weak instruments by computing the F-statistics of those instruments. The reported F-statistics for the joint explanatory of the instrumental variables is 1546.81, which well

exceeds the threshold value of 10 suggested by Staiger and Stock (1997). Furthermore, the p-value of the Cragg-Donald's Wald F weak-instrument test statistic is 0.000, rejecting the null hypothesis that the instruments are weak (Cragg and Donald 1993; Stock and Yogo 2005). In addition, Hansen's J overidentification test shows a p-value of 0.5160, implying that the two instruments are valid and uncorrelated with the error term (Hansen 1982).

In column (2), we report the results of the second-stage regressions for *Signed Discretionary Accruals, SDA.* The coefficient on predicted *Cultural Similarity* estimated from the first regression is significantly positively associated with *SDA*, similar to the main results in **Table 4.5**, implying that our results are robust to endogeneity concerns.

Table 4. 6: Endogeneity test – instrumental variables regression

This table reports instrumental variables regression estimation results. Column (1) reports the first-stage results of the 2SLS regressions with *Cultural Similarity* as the dependent variable. Accrual-based earnings management is measured as *Signed Discretionary Accruals (SDA)*. *Cultural Similarity* is the proportion of board directors that share similar ethnicity with the *CEO. Malaysia Small Town* is a dummy variable which equals one if a firm is headquartered outside of a large metropolitan area and zero, otherwise. Column (2) reports the second-stage results from 2SLS regressions for *SDA*, respectively. All other variables are defined in **Table 4.2**. Standard errors are clustered at the firm level and t-statistics are reported in parentheses. ***, **, * indicate significance at the 1%, 5% and 10% level, respectively.

	First stage	**Second Stage**
	Cultural Similarity	***Signed Discretionary Accrual (SDA)***
	(1)	**(2)**
Malaysia Small Town	0.053***	
	(5.93)	
Cultural Similarity		0.029**
		(2.577)
Board Independence	-0.094***	0.082***
	(-2.89)	(2.717)
Board Meeting	0.021	-0.023*
	(1.53)	(-1.946)
Board Size	0.022	0.004
	(1.31)	(0.302)
Leverage	0.081*	0.016
	(1.94)	(0.455)
Firm Age	-0.001***	-0.000
	(-6.57)	(-0.249)
Firm Size	-0.020***	0.003
	(-5.86)	(0.817)
Sales Growth	0.000	0.000
	(1.29)	(0.646)
Market-to-Book Ratio	0.000	-0.000**
	(0.67)	(-2.566)
ROA	-0.045	0.233***
	(-0.95)	(5.899)
Return Volatility	-0.000	0.000
	(-1.37)	(0.533)
Big4 Auditor	0.010	-0.005
	(1.21)	(-0.715)
Intercept	0.784***	-0.053
	(14.25)	(-0.434)
Industry FE	Yes	Yes
Year FE	Yes	Yes
Observations	3588	3,050
R-squared	0.134	0.023
Cragg-Donald Wald F Statistic	1546.81	
Hansen J p-value	0.5160	

4.4.2.2 Endogeneity test using Propensity Score Matching

We also employ a matching approach and apply propensity score matching techniques to mitigate concerns relating to self-selection (Rosenbaum and Rubin 1983; Shipman et al. 2017) and 'sample selection bias' that is triggered by observable factors (Dehejia and Wahba 2002). For instance, CEOs with high demographic similarity to directors are more prone to appoint similar directors (e.g., directors who share the same ethnicity) (Westphal and Zajac 1995) which affects the firm value.

We compare the firm value in firms with high cultural similarity (i.e., treatment firms) and a sample of control firms with low cultural similarity (i.e., control firms). We define the treatment firms as firms with an above-sample mean fraction of CEO-board cultural similarity and control firms as firms with a below-sample-mean fraction of CEO-board cultural similarity.

The propensity score matching method proceeds in two steps. First, we estimate a probit[14] model using the full sample to compute the probability (i.e., the propensity score) that a firm with a set of firm-level characteristics is run by the treatment firms. We use the same controls as those included in the baseline regression. The probit regression results are reported in column (1) in Panel A of **Table 4.7**. We find that firms with high cultural similarity are slightly larger, older, less leveraged, and have lower market-to-book ratio than their counterparts with low cultural similarity.

To ensure that firms in the treatment sample and control sample are comparable, we employ the nearest neighbour approach. Specifically, each firm with high cultural similarity is matched to a firm with a low cultural similarity that has the closest propensity score. In our matching, we require the maximum difference between the propensity scores of the firm with high and that with low cultural similarity to not exceed 0.1% in absolute value.

Next, we employ two diagnostic analyses to verify that firms in the treatment and control groups are indistinguishable in terms of observable characteristics. First, we re-estimate the probit model for the post-match sample. Column (2) in Panel A shows that all of the estimated coefficients are statistically insignificant except the coefficient on market-to-book ratio, implying the absence of any distinguishable trends in

[14] We also use a logit model in the first step as an alternative test and the results are qualitatively similar.

earnings management between the two groups. In addition, the estimated coefficients in column (2) are smaller in magnitude than those in column (1), signifying that the decrease in statistical significance is not simply driven by reduced sample size. Lastly, **Table 4.7** shows a decrease in pseudo-R-squared from 0.030for the pre-match sample to 0.002 for the post-match sample. This implies that propensity score matching eliminates all observable differences other than those related to cultural similarity.

Second, we examine the differences for each observable characteristic between the treatment firms and the matched control firms. All univariate difference tests in Panel B of **Table 4.7** are statistically insignificant, indicating that the differences in firm value between the treatment and control groups are only due to the presence of cultural similarity.

Panel C of **Table 4.7** presents the propensity score matching estimates. The results indicate that there are insignificant differences, at the 1% level, in firm value between firms with high and those with low cultural similarity

Finally, we re-estimate the baseline model by using treatment and matched control sample and reports the result in Panel D of **Table 4.7**. Nevertheless, the results show that the coefficient on *Cultural Similarity* is positive but insignificant in all specification. Thus, the propensity score matching results are inconsistent with those in the baseline specification, implying that our main findings are likely to be influenced by omitted variables related to nonlinear forms of our control variables.

Table 4. 7: Propensity score matching estimates

This table reports the propensity score matching estimation results. Panel A reports estimates from the probit model used to estimate propensity scores. The dependent variable is a dummy variable that equals one for firms with high *Cultural Similarity*, and zero otherwise. We define a firm with high CEO-board cultural similarity (treatment firms) if it has an above-sample mean fraction of CEO-board cultural similarity and a firm with low CEO-board cultural similarity (control firms) if it has below-sample-mean fraction of CEO-board cultural similarity. All independent variables are defined in **Table 4.2**. Industry dummies are constructed based on the two-digit SIC code classification. Panel B reports the univariate comparisons of firm characteristics and board characteristics between treatment group and control group. Panel C reports the average treatments estimates. Panel D reports the regression results using PSM procedure. ***, **, and * indicate significance at the 1%, 5%, and 10% level, respectively.

Panel A: Pre-match propensity score regression and post-match diagnostic regression

	High Cultural Similarity Dummy	
	(1)	**(2)**
	Pre-Match	**Post-Match**
Board Independence	-0.206	-0.058
	(-1.238)	(-0.296)
Board Size	0.096	0.001
	(1.357)	(0.016)
Board Meeting	-0.105	-0.036
	(-1.173)	(-0.346)
Leverage	0.062	-0.065
	(0.298)	(-0.266)
Firm Age	-0.004***	-0.001
	(-3.752)	(-0.778)
Firm Size	-0.107***	-0.010
	(-6.211)	(-0.468)
Sales Growth	0.002	0.002
	(0.779)	(1.261)
Market-to-book ratio	-0.000***	-0.000**
	(-4.084)	(-2.272)
Return on Assets	0.347*	0.215
	(1.697)	(0.800)
Return Volatility	-0.002	-0.001
	(-1.138)	(-0.357)
Big4 Auditor	-0.001	0.044
	(-0.018)	(0.872)
Intercept	0.947***	0.204
	(4.194)	(0.770)
Observations	4.368	3,565
Pseudo R^2	0.030	0.002
Industry FE	Yes	Yes
Year FE	Yes	Yes

Panel B: Differences in the firm and board characteristics

	Firm-year obs. with high CEO-board cultural similarity	Firm-year obs. with low CEO-board cultural similarity	Difference	*t*-stat
	(N=2212)	(N=2180)		
Board Independence	0.4632	0.4662	-0.003	-0.77
Board Meeting	1.6338	1.604	0.0298	-0.78
Board Size	1.942	1.9413	0.0007	0.09
Leverage	0.0702	0.0721	-0.0018	-0.58
Firm Age	28.561	28.244	0.317	0.54
Firm Size	5.5986	5.5632	0.0354	0.78
Sales Growth	0.5134	0.1391	0.3743	1.35
Market-to-book ratio	743.29	853.31	-110.02	-1.56
Return on Asset	0.0333	0.0307	0.0026	0.99
Return volatility	11.627	11.985	-0.358	-0.86
Big4 Auditor	0.4359	0.4269	0.0089	0.59

Panel C: Propensity score matching estimator

Variables	Firm-year obs. with high CEO-board cultural similarity	Firm-year obs. with low CEO-board cultural similarity	Difference	T-stat
AAC	-0.0008	-0.0026	0.00182	0.33
ATT	-0.00008	0.00026	-0.00109	-0.19

Panel D: The regression results using PSM procedure

	Signed Discretionary Accrual (SDA)		
	(1)	**(2)**	**(3)**
Cultural Similarity	0.012	0.013	0.015
	(0.814)	(0.845)	(0.972)
Board Independence			0.064*
			(1.706)
Board Meeting			-0.019*
			(-1.773)
Board Size			-0.007
			(-0.614)
Leverage		0.010	0.016
		(0.320)	(0.529)
Firm Age		0.000	-0.000
		(0.138)	(-0.237)

Firm Size		-0.003	-0.001
		(-0.909)	(-0.395)
Sales Growth		0.000	0.000
		(0.719)	(0.558)
Market-to-Book Ratio		0.000	0.000
		(0.660)	(0.711)
ROA		0.194***	0.201***
		(4.660)	(4.924)
Return Volatility		0.000	0.000
		(0.106)	(0.108)
Big4 Auditor		-0.006	-0.005
		(-1.156)	(-1.021)
Intercept	-0.008	-0.001	0.005
	(-0.839)	(-0.047)	(0.164)
Industry FE	Yes	Yes	Yes
Year FE	Yes	Yes	Yes
Observations	3,565	3,565	3,565
R-squared	0.0002	0.0099	0.0240

4.4.2.3 Endogeneity test using Heckman selection model

A firm's decision to appoint a CEO with higher cultural ties with board of directors may be non-random and this may cause a self-selection bias. Thus, to address this concern, we conduct the Heckman two-step sample selection model as robustness check. In the first stage model, we compute the inverse Mills ratio from a probit model that captures the determinants of firms appointing CEO with similar cultural ties with board of directors. In particular, this probit model controls for a dummy variable (*Malaysia Small Town*) for whether a firm is headquartered outside of a large town in Malaysia. The motivation to use this exogenous variable is that we assume firms headquartered in these areas are to be less culturally diverse than firms headquartered in large towns (Anderson et al. 2011; Frijns et al. 2016). Furthermore, Heckman's estimator requires exogenous variable that is correlated with a firm's propensity to appoint CEO with similar cultural background with board of directors, but not with earnings management. Thus, the *Malaysia Small Town* is likely to be an important factor for a firm to appoint CEO that has higher cultural similarity with board of directors.

We also control for *Board Independence, Board Meeting, Board Size, Leverage, Firm Age, Firm Size, Sales Growth, Market-to-Book Ratio, ROA, Return Volatility* and *Big4 Auditor*. In the second stage, we include the inverse Mills ratio which is generated from first stage into the regression model as an additional control variable to control for the potential sample selection bias.

The results of the first-step regression in Column (1) of **Table 4.8** show that *Malaysia Small Town* and *Board Size* have significant and positive impacts on the CEO-board cultural similarity, whereas *Board Independence, Firm Size, Firm Age and Market-to-Book* have significantly negative impacts.

The results of the second-step regression in Column (2) of **Table 4.8** show that the coefficient on *Cultural Similarity* remain significantly positive. The coefficient on *Inverse Mills Ratio* is positive and insignificant.

Overall, our reported findings in **Table 4.8** are qualitatively similar to our results reported under the main analysis and hence implying that our results reported under the main analysis do not appear to be driven sample selection bias.

Table 4. 8: Heckman two-stage analysis

This table reports the regression results of Heckman model. The first step is a probit model with a binary cultural similarity dummy. *Dummy Cultural Similarity* equals one if the firm has an above-sample mean fraction of CEO-board cultural similarity and zero, otherwise. *Malaysia Small Town* is an exogenous variable, which equals one if the firm is headquartered in small towns and zero, otherwise. The second stage is ordinary least square regression of the impact of CEO-board cultural similarity on firm value. *Inverse Mills Ratio* is generated from the first step and included in the second step of this model. All other variables are defined in **Table 4.2**. Standard errors are clustered at the firm level and t-statistics are reported in parentheses. ***, **, * denote statistical significance at the 1%, 5%, and 10% level, respectively.

	First-step regression	Second-step regression
	Dummy Cultural similarity	***Signed Discretionary |Accruals (SDA)***
Cultural similarity		0.060**
		(2.557)
Malaysia Small Town	0.401***	
	(9.330)	
Board Independence	-0.310*	0.090**
	(-1.886)	(2.370)
Board Meeting	0.063	-0.031*
	(0.935)	(-1.955)
Board Size	0.164*	-0.007
	(1.866)	(-0.336)
Leverage	0.109	0.063
	(0.548)	(1.279)
Firm Age	-0.003***	0.000
	(-2.850)	(0.135)
Firm Size	-0.073***	0.001
	(-4.404)	(0.232)
Sales Growth	0.010	0.000
	(1.067)	(0.587)
Market-to-book ratio	-0.000***	0.000
	(-3.486)	(1.225)
ROA	0.295	0.383***
	(1.234)	(6.441)
Return Volatility	-0.002	0.002***
	(-1.185)	(6.787)
Big4 Auditor	0.078*	0.005
	(1.834)	(0.565)
Inverse Mills Ratio		0.022
		(0.537)
Intercept	0.176	-0.107
	(0.796)	(-1.342)
Industry FE	Yes	Yes
Year FE	Yes	Yes
Observations	4,513	4,513
Pseudo R2	0.031	
Adjusted R2		0.036

4.4.2.3 Alternative proxy for earnings management

To further explore the effect of CEO-board cultural similarity on earnings management, we examine real earnings management as an alternative measure of earnings management. To effectively detect real earnings management, we employ three real activities-based earnings management measures (Rowchowdhury 2006; Cohen et al. 2008; Cohen and Zarowin 2010). These measures are based on the abnormal level of operating cash flows (*AB_CFO*), abnormal level of production costs (*AB_PROD*), and abnormal level of discretionary expenses as proxies for real earnings management (*AB_DIS*). The abnormal levels of real activities are the differences between actual values and the normal levels calculated using the estimated coefficient from the cross-sectional regression estimated by the following models by industry (at the 1-digit SIC level) and year, in which there are at least 15 observations for each industry-year combination in Eqs. (**4.4**)-(**4.6**). Then we use these three measures as proxies for real earnings management in this study.

$$\frac{CFO_{i,t}}{A_{i,t-1}} = \beta_0 + \beta_1 \frac{1}{A_{i,t-1}} + \beta_2 \frac{S_{i,t}}{A_{i,t-1}} + \beta_3 \frac{\Delta S_{i,t}}{A_{i,t-1}} + \varepsilon_t \qquad (\mathbf{4.4})$$

$$\frac{COST_{i,t}}{A_{i,t-1}} = \beta_0 + \beta_1 \frac{1}{A_{i,t-1}} + \beta_2 \frac{S_{i,t}}{A_{i,t-1}} + \beta_3 \frac{\Delta S_{i,t}}{A_{i,t-1}} + \beta_4 \frac{\Delta S_{i,t-1}}{A_{i,t-1}} + \varepsilon_t \qquad (\mathbf{4.5})$$

$$\frac{EXP_{i,t}}{A_{i,t-1}} = \beta_0 + \beta_1 \frac{1}{A_{i,t-1}} + \beta_2 \frac{S_{i,t-1}}{A_{i,t-1}} + \varepsilon_t \qquad (\mathbf{4.6})$$

where $CFO_{i,t}$ is net cash flow from operations of firm *i* for period *t*; $COST_{i,t}$ is production cost, defined as the sum of the cost of goods sold and the change in inventories of firm *i* for period *t*; $EXP_{i,t}$ is the sum of sales expense and administrative expense of firm *i* for period *t*; $S_{i,t}$ is revenues of firm *i* for period *t*; $\Delta S_{i,t}$ is the change in revenues of firm *i* for period *t*; and $\Delta S_{i,t}$ is a change in revenues of firm *i* for period *t-1*. $A_{i,t-1}$ is total assets of firm *i* at the end of period *t-1*. All the variables are scaled by $A_{i,t-1}$. For the sake of clarity, we multiply both abnormal cash flows from operations and abnormal discretionary expenditures by negative one so they can represent real earnings management in a consistent approach with the value of abnormal production cost.

Consistent with Cohen and Zarowin (2010) and Cohen et al. (2008), we also use the absolute value of the following three aggregate measures of real earnings

management, *REM1*, *REM2*, and *REM3*, to capture the total amount of real earnings management engaged by the firm in a particular fiscal year:

$$REM1 = AB\_DIS + AB\_PROD$$

$$REM2 = AB\_CFO + AB\_DIS$$

$$REM3 = AB\_PROD - AB\_CFO - AB\_DIS$$

Table 4.9 presents our analysis of the impact of CEO-board cultural similarity on real earnings management. We estimate separate regressions using the three subcomponents of real earnings management separately as dependent variables and report the results in columns (1), (2), and (3), respectively. The results indicate that CEO-board cultural similarity (*Cultural Similarity*) is positively associated with abnormal production costs, *AB_PROD* (b=0.022, t=2.084). Meanwhile, we find no significant association between CEO-board cultural similarity and abnormal cash flow (*AB_CFO*), or abnormal discretionary expenses (*AB_DIS*). Taken together, the results show that firms with a higher fraction of *Cultural Similarity* are more likely to engage in real-activities earnings management through production activities rather than sales and discretionary expenses manipulation activities. Next, columns (4), (5), and (6) report the regression results of our three-aggregate metrics, *REM1*, *REM2*, and *REM3*, as dependent variables, respectively. In columns (4) and (6), the coefficients on *Cultural Similarity* and aggregate metric of real earnings management, *REM1* and *REM3*, are both positive and significant at the 10% level, implying that CEO-board cultural similarity is associated with increased real earnings management.

As for control variables, the relationship between *Board Independence* and *REM3* is negative and significant at the 5% level, indicating that firms with a higher fraction of board independence engage in less real-activities management. In addition, *Board Size* is significantly and negatively associated with *REM3*, indicating that firms with larger board size are less likely to engage in real-activities earnings management. We also find that larger firms are prone to engage in real earnings management and that firms with better performance and higher market-to-book ratio are less likely to engage in real earnings management. Finally, there is also evidence that firms with higher return volatility are more likely to engage in real earnings management. Overall, our results on control variables are consistent with prior studies (Cheng et al. 2016; Kim et al. 2017; Cai et al. 2019).

Thus, **Table 4.9** shows that our main findings are robust to this alternative measure of earnings management, i.e., real earnings management. The results support the notion that firms with a higher fraction of CEO-board cultural similarity are more prone to engage in real earnings management, consistent with our results for accrual-based management.

Table 4. 9: CEO-board cultural similarity and real earnings management

This table reports the OLS estimation results of real earnings management on a measure of CEO-board cultural similarity, board characteristics, and firm characteristics for Malaysian non-financial listed firms in the sample period of 2009 to 2016. *Cultural Similarity* is the proportion of board directors that share similar ethnicity with the CEO. All other variables are defined in **Table 4.2**. Standard errors are clustered at the firm level and t-statistics are reported in parentheses. ***, **, * indicate statistical significance at the 1%, 5%, and 10% level, respectively.

	AB_CFO	***AB_PROD***	***AB_DIS***	***REM1***	***REM2***	***REM3***
	(1)	**(2)**	**(3)**	**(4)**	**(5)**	**(6)**
Cultural Similarity	-0.008	0.022**	-0.006	0.016*	-0.014	0.035*
	(-0.935)	(2.084)	(-0.774)	(1.661)	(-1.228)	(1.886)
Board Independence	-0.027	0.030	-0.031**	-0.000	-0.058***	0.088**
	(-1.597)	(1.488)	(-2.167)	(-0.020)	(-2.644)	(2.398)
Board Meeting	-0.009	0.001	0.008	0.010	-0.001	0.002
	(-1.298)	(0.151)	(1.391)	(1.202)	(-0.108)	(0.148)
Board Size	-0.001	-0.042***	0.018**	-0.023**	0.017	-0.058***
	(-0.155)	(-3.842)	(2.433)	(-2.311)	(1.456)	(-2.996)
Leverage	-0.055**	0.004	0.043**	0.047**	-0.012	0.016
	(-2.576)	(0.159)	(2.414)	(1.974)	(-0.438)	(0.349)
Firm Age	0.000	-0.001***	0.000***	-0.000	0.000***	-0.001***
	(0.182)	(-4.255)	(4.386)	(-1.294)	(2.983)	(-4.134)
Firm Size	-0.002	0.016***	-0.008***	0.008***	-0.010***	0.026***
	(-1.305)	(7.456)	(-5.348)	(4.016)	(-4.479)	(6.799)
Sales Growth	-0.000	0.000	0.000	0.000	0.000	0.000
	(-0.073)	(0.968)	(0.149)	(1.152)	(0.039)	(0.513)
Market-to-Book	0.000***	-0.000***	-0.000	-0.000***	0.000***	-0.000***
	(6.033)	(-6.915)	(-1.143)	(-8.287)	(3.947)	(-6.183)
ROA	0.206***	-0.391***	-0.045***	-0.435***	0.161***	-0.552***
	(10.727)	(-16.987)	(-2.785)	(-20.339)	(6.531)	(-13.305)
Return Volatility	-0.000**	0.000	-0.000	0.000	-0.001**	0.001**
	(-2.065)	(1.416)	(-1.229)	(0.603)	(-2.401)	(2.214)
Big4 Auditor	0.009**	-0.005	-0.016***	-0.021***	-0.007	0.003
	(2.042)	(-0.888)	(-4.435)	(-4.270)	(-1.286)	(0.273)
Intercept	0.085***	-0.079**	0.011	-0.069**	0.096***	-0.175***
	(2.982)	(-2.323)	(0.444)	(-2.164)	(2.605)	(-2.838)
Industry FE	Yes	Yes	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes	Yes	Yes
Observations	4,346	4,346	4,346	4,346	4,346	4,346
R-squared	0.0958	0.2207	0.1388	0.1950	0.1267	0.2052

4.4.3 Additional analyses

4.4.3.1 Controlling for CEO duality

We further investigate the possibility that firms with a higher fraction of cultural similarity consist of more powerful CEOs. Prior studies suggest that entrenched CEOs can abuse their power to manipulate earnings numbers in order to maintain their position or increase their compensation (Healy and Wahlen 1999). In this study, we use CEO duality as a proxy for CEO power. CEO duality is measured when the same person holds the CEO and board chair position in a firm. The dual leadership structure may challenge the board's ability to effectively monitor and discipline the CEO, thus CEOs may use it as a management entrenchment tool (Goyal and Park 2002; Adams et al. 2005).

Hence, we examine whether CEO duality influences earnings management. In **Table 4.10**, we include *Duality* as an additional regressor in all of our regressions. *Duality* equals one if the CEO also serves as chair of the board, and zero otherwise. We find the estimated coefficients on *Cultural Similarity* for *SDA*, AB_*PROD* and *REM3* continue to be significantly positive after controlling for CEO duality, implying that the main results in **Table 4.5** hold after controlling for CEO power. Nevertheless, the coefficient on *Duality* is insignificant for both *SDA* (Column 1) and *AB_DIS* (Column 4), significantly positive for *AB_CFO* (Column 2), and significantly negative for *AB_PROD* (Column 3).

These findings suggest that firms with a dual leadership structure or with more power CEOs are more likely to engage in real-earning management through sales manipulations activities and less likely to engage in real earnings management through production activities. Meanwhile, column (5) shows that the coefficient on *Duality* is significantly negatively associated with an aggregate measure of real earnings management, *RM3*, indicating that firms with a dual leadership structure or more powerful CEOs are less likely to engage in real-activities earnings management.

Table 4. 10: Controlling CEO duality (CEO power)

This table reports the OLS estimation results of accrual-based earnings management and real earnings management on a measure of CEO-board cultural similarity, CEO duality (*Duality*), board characteristics, and firm characteristic for Malaysian non-financial listed firms in the sample period of 2009 to 2016. *Cultural Similarity* is the proportion of board directors that share similar ethnicity with the CEO. All other variables are defined in **Table 4.2.** Standard errors are clustered at the firm level and t-statistics are reported in parentheses ***, **, * indicate statistical significance at the 1%, 5%, and 10% level, respectively.

	SDA	***AB_CFO***	***AB_PROD***	***AB_DIS***	***REM3***
	(1)	**(2)**	**(3)**	**(4)**	**(5)**
Cultural Similarity	0.032**	-0.010	0.024**	-0.006	0.039**
	(2.292)	(-1.121)	(2.274)	(-0.825)	(2.098)
Duality	-0.011	0.012*	-0.019**	0.005	-0.036***
	(-1.073)	(1.929)	(-2.493)	(0.862)	(-2.608)
Board Independence	0.081***	-0.026	0.028	-0.030**	0.084**
	(2.981)	(-1.511)	(1.378)	(-2.125)	(2.283)
Board Meeting	-0.023**	-0.009	0.001	0.008	0.001
	(-2.020)	(-1.241)	(0.098)	(1.401)	(0.088)
Board Size	0.003	-0.001	-0.043***	0.019**	-0.062***
	(0.219)	(-0.059)	(-3.997)	(2.495)	(-3.151)
Leverage	0.016	-0.053**	0.002	0.043**	0.012
	(0.453)	(-2.500)	(0.083)	(2.430)	(0.265)
Firm Age	-0.000	0.000	-0.001***	0.000***	-0.001***
	(-0.450)	(0.212)	(-4.344)	(4.417)	(-4.210)
Firm Size	0.004	-0.002	0.016***	-0.008***	0.027***
	(1.223)	(-1.372)	(7.558)	(-5.383)	(6.902)
Sales Growth	0.000	-0.000	0.000	0.000	0.000
	(0.630)	(-0.043)	(0.930)	(0.162)	(0.473)
Market-to-Book Ratio	-0.000**	0.000***	-0.000***	-0.000	-0.000***
	(-2.571)	(6.048)	(-6.938)	(-1.134)	(-6.207)
ROA	0.234***	0.207***	-0.392***	-0.044***	-0.554***
	(5.926)	(10.764)	(-17.026)	(-2.768)	(-13.352)
Return Volatility	0.000	-0.000**	0.000	-0.000	0.001**
	(0.547)	(-2.081)	(1.439)	(-1.236)	(2.237)
Big4 Auditor	-0.005	0.009**	-0.005	-0.016***	0.002
	(-0.755)	(2.085)	(-0.965)	(-4.396)	(0.197)
Intercept	-0.057	0.083***	-0.075**	0.009	-0.168***
	(-1.239)	(2.903)	(-2.191)	(0.389)	(-2.707)
Industry FE	Yes	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes	Yes
Observations	3,581	4,339	4,339	4,339	4,339
R-squared	0.0243	0.0966	0.2218	0.1390	0.2064

4.4.3.2 Board independence and earnings management

From the agency theory perspective, boards that are mainly constituted of a majority of independent directors or outside directors are more likely to effectively monitor the management. Even several policies introduced in many jurisdictions such as MCCG 2000 and the Cadbury Committee Report in England (1999) have presumed that board independence can enhance the effectiveness of the board. The effectiveness of independent directors in their monitoring function can strengthen the internal control, and thereby contribute towards the integrity of financial reporting.

Yet, prior evidence on the link between board independence and earnings management is mixed (Klein 2002; Bédard et al. 2004; Agrawal and Chadha 2005; Vafeas 2005; Larcker et al. 2007; Chen et al. 2015). For instance, using a sample of publicly-traded US firm years, Klein (2002) finds a negative relationship between board independence and earnings management. Later studies (e.g., Bédard et al. 2004) also find that both independent directors and audit committees improve monitoring by reducing earnings management. Notwithstanding this, others, such as Agrawal and Chadha (2005), Vafeas (2005), and Larcker et al. (2007), find no evidence on the relationship between board/audit committee independence and earnings management.

Another strand of literature also argues that the conventionally defined board independence does not account for the presence of social ties and pre-existing network connections between CEOs and independent directors, which are associated with weaker internal governance (Hwang and Kim 2009; Krishnan et al. 2011) that could also affect the integrity of reported earnings (Hwang and Kim 2012). Thus, motivated by these prior studies, we propose a culturally-adjusted measure of board independence to investigate the extent to which the cultural independence between CEO and independent directors is relevant to earnings management practice.

To investigate the relevance of the cultural ties, we investigate the differential association between board independence and the income-increasing earnings management when we incorporate the conventional definition of board independence with our proposed cultural independence. If cultural ties do not matter, then the results will show no differential association between board independence and the income-increasing earnings management when we replace the conventional board independence measure with our proposed measure of board independence.

To analyse this case, we construct a *Conventionally Independent Board Dummy (CIB)* that equals one if there is a majority of directors who are classified as independent based on conventional definitions (i.e., based on the Malaysian Code on Corporate Governance), and zero otherwise. We then construct a *Culturally Adjusted Independent Board Dummy* (*AIB*) that equals one when more than half of the board comprises directors who are both conventionally and culturally independent (i.e., those who have no cultural ties with the CEO), and zero otherwise. Similar to our main analysis, we use *SDA* as a proxy for income-increasing earnings management.

The results in **Table 4.11** suggest a significant differential relation between board independence and the income-increasing earnings management when we replace the formal measure of board independence, *CIB* (which does not incorporate cultural ties), with our new measure, *AIB* (which does incorporate cultural ties). Column (1) shows that the coefficient on *CIB* is negative and insignificant, implying that there is no significant association between conventional board independence and income-increasing earnings management.

Meanwhile, column (2) shows that the coefficient on our newly proposed independent measure, *AIB*, is significant and negative (b=-0.031, $p<.1$), implying that firms with the majority of directors who are both conventionally and culturally independent are less likely to engage in income-increasing earnings management. The negative effect of board independence on income-increasing (accrual-based) earnings management is evident in a truly independent board, i.e., board members do not have any formal or cultural ties with the CEO. The results indicate that boards are more effective at controlling agency issues and limiting managerial opportunism when they are both conventionally and culturally independent of the CEO.

As for the control variables, we also find that the coefficient on *Board Meeting* is negative and statistically significant at the 5% level, implying that firms engage less in income-increasing earnings management when there is a higher frequency of board meetings, which is consistent with Xie et al. (2003). We also find that the coefficient on *Market-to-Book Ratio* is negative and significant at the 1% level, indicating that firms with high growth opportunities are associated with reduced income-increasing earnings management (accrual-based). The results also show that coefficients on both *ROA* and *Return Volatility* are positive and significant, implying that firms with high

profitability are more likely to engage income-increasing earnings management (accrual-based), which is in line with Chung et al. (2002).

Table 4. 11: Board independence and earnings management

This table exhibits OLS regression estimation results of the accrual-based earnings management measure on board and firm characteristics of Malaysian non-financial listed firms in the sample period of 2009 to 2016. Accrual-based earnings management is measured as *Signed Discretionary Accrual (SDA). Conventionally Independent Board Dummy (CIB)* is classified as a dummy that equals one if a majority of directors are classified as independent as specified by current regulations, and zero otherwise. *Culturally Adjusted Independent Board Dummy* (*AIB)* is a dummy that equals one if the board consists of directors that are both formally and culturally independent, and zero otherwise. All other variables are defined in **Table 4.2**. Standard errors are clustered at the firm level and t-statistics are reported in parentheses. ***, **, * denote statistical significance at the 1%, 5%, and 10% level, respectively.

	Signed Discretionary Accrual (SDA)	
	(1)	**(2)**
Conventionally Independent Board (CIB)	-0.010	
	(-0.927)	
Culturally Adjusted Independent Board (AIB)		-0.031*
		(-1.816)
Board Meeting	-0.021**	-0.023**
	(-2.035)	(-2.177)
Board Size	-0.000	0.001
	(-0.035)	(0.092)
Duality	-0.005	-0.006
	(-0.546)	(-0.694)
Leverage	0.029	0.027
	(0.941)	(0.885)
Firm Age	-0.000	-0.000
	(-0.353)	(-0.099)
Firm Size	0.004	0.004
	(1.398)	(1.543)
Sales Growth	0.000	0.000
	(0.489)	(0.488)
Market-to-Book Ratio	-0.000***	-0.000***
	(-2.761)	(-2.723)
ROA	0.297***	0.299***
	(8.206)	(8.251)
Return Volatility	0.002***	0.002***
	(7.491)	(7.489)
Big4 Auditor	-0.002	-0.002
	(-0.376)	(-0.345)
Intercept	-0.062	-0.052
	(-1.447)	(-1.302)
Industry FE	Yes	Yes
Year FE	Yes	Yes
Observations	4,169	4,169
R-squared	0.0396	0.0401

4.4.3.3 Independent versus dependent (executive) directors

As an additional test of the relevance of cultural ties, we examine whether the negative effect of cultural similarity on earnings management is equal when this similarity is measured among dependent (executive) or independent directors. According to prior literature (Fama 1980; Fama and Jensen 1983; Weisbach 1988), independent directors serve as effective monitors of senior managers and perform an important monitoring function, while executive directors have mainly an advisory role. However, the question remains as to whether cultural similarity diminishes the monitoring effectiveness of independent directors that could be reflected in the practice of earnings management.

If we discover that independent directors who share a similar cultural background with the CEO are also weak monitors, then it would suggest that the independence measure traditionally employed in the prior literature does not encapsulate the inclination of the board to provide effective oversight and monitoring. Given that independent directors have a stronger focus on monitoring, we argue that cultural similarity is more detrimental to that role and CEOs who share a similar cultural background with independent directors are prone to engage in earnings management.

To analyse this, we further construct two new measures of cultural similarity. The first variable is the *Cultural Similarity-Independent*, which is defined as the proportion of the board that consists of directors that share a similar cultural background with the CEO and are independent. The second variable is the *Cultural Similarity-Dependent/Executive*, which is defined as the proportion of the board that consists of directors that share a similar cultural background with the CEO and are executive/non-independent. These two measures are constructed to investigate whether the negative effect of cultural similarity on earnings management is equal between directors who are affiliated versus those who are supposedly independent

First, we analyse the impact of *Cultural Similarity-Independent* on *SDA* and report the results in **Table 4.12**. Column (1) shows that the coefficient on *Cultural Similarity-Independent* is positive (*b=0.031*) and significant at the 10% level. However, column (2) shows that the coefficient on *Cultural Similarity-Dependent*/*Executive* is positive but statistically insignificant. Therefore, our study reveals that cultural ties within the

CEO-board relationship weaken the effectiveness of board independence and impair earnings quality.

The positive effect of CEO-board cultural similarity on income-increasing accrual-based earnings management is more concentrated among boards with formally independent directors, as cultural ties may prevent conventionally independent directors from performing their monitoring function. Our results suggest that cultural similarity prevents independent directors from performing their monitoring role effectively. Furthermore, we suggest that, once a director has cultural ties with the CEO, the independence of the director does not matter from a monitoring perspective. This could be an explanation for why the literature has shown equivocal evidence on the relation between board independence and earnings management (Park and Shin 2004; Peasnell and Young 2005; Chen et al. 2015).

We further test whether the impact of cultural similarity on real earnings management hinges upon whether the directors are independent or executive. We re-estimate our regression model with the inclusion of the two new variables to examine the impact of *Cultural Similarity-Independent* and *Cultural Similarity-Dependent/Executive* on measures of real earnings management and report the results in **Table 4.13**. Columns (1) and (3) show that the coefficient of *Cultural Similarity-Independent* is statistically insignificant, implying that cultural similarity between CEO and independent directors does not cause abnormal cash flow and production activities.

Nevertheless, column (5) shows that the coefficient on *Cultural Similarity-Independent* is negative and statistically significant at the 5% level, implying firms with a higher fraction of shared cultural similarity between CEOs and independent directors are less likely to engage in abnormal levels of discretionary accruals. Meanwhile, columns (2), (4), and (6) show that the coefficient on *Cultural Similarity-Independent* is statistically insignificant, indicating that firms with a higher fraction of shared cultural similarity between CEOs and dependent directors (executive) are not associated with real earnings management.

Table 4. 12: Accrual-based earnings management: independent versus dependent directors

This table exhibits OLS regression estimation results of the accrual-based earnings management measure on board and firm characteristics of Malaysian non-financial listed firms in the sample period of 2009 to 2016. Accrual-based earnings management is measured as *Signed Discretionary Accrual (SDA). Cultural Similarity-Independent* and *Cultural Similarity-Dependent/Executive* are the measures of CEO-board cultural similarity computed for dependent/executive and independent directors. All other variables are defined in **Table 4.2**. Standard errors are clustered at the firm level and t-statistics are reported in parentheses. ***, **, * denote statistical significance at the 1%, 5%, and 10% level, respectively.

	Signed discretionary accrual (SDA)	
	(1)	**(2)**
Cultural Similarity-Independent	0.031*	
	(1.816)	
Cultural Similarity-Dependent/Executive		0.001
		(0.201)
Board Independence	0.050*	0.072***
	(1.864)	(2.850)
Board Meeting	-0.023**	-0.021**
	(-2.177)	(-2.042)
Board Size	0.001	-0.001
	(0.092)	(-0.051)
Duality	-0.006	-0.005
	(-0.694)	(-0.558)
Leverage	0.027	0.028
	(0.885)	(0.930)
Firm Age	-0.000	-0.000
	(-0.099)	(-0.292)
Firm Size	0.004	0.004
	(1.543)	(1.374)
Sales Growth	0.000	0.000
	(0.488)	(0.481)
Market-to-Book Ratio	-0.000***	-0.000***
	(-2.723)	(-2.759)
ROA	0.299***	0.297***
	(8.251)	(8.203)
Return Volatility	0.002***	0.002***
	(7.489)	(7.477)
Big4 Auditor	-0.002	-0.002
	(-0.345)	(-0.369)
Intercept	-0.052	-0.050
	(-1.302)	(-1.226)
Industry FE	Yes	Yes
Year FE	Yes	Yes
Observations	4,169	4,169
R-squared	0.0401	0.0394

Table 4. 13: Real earnings management: independent versus dependent directors

This table exhibits OLS regression estimation results of real earnings management measures on board and firm characteristics of Malaysian non-financial listed firms in the sample period of 2009 to 2016. *Cultural Similarity-Independent* and *Cultural Similarity-Dependent/Executive* are the measures of CEO-board cultural similarity computed for dependent and independent directors. All other variables are defined in **Table 4.2**. Standard errors are clustered at the firm level and t-statistics are reported in parentheses. ***, **, * denote statistical significance at the 1%, 5%, and 10% level, respectively.

	AB_CFO		***AB_PROD***		***AB_DIS***	
	(1)	**(2)**	**(3)**	**(4)**	**(5)**	**(6)**
Cultural Similarity-Independent	-0.010		0.008		-0.018**	
	(-0.995)		(0.628)		(-2.027)	
Cultural Similarity-Dependent/Executive		0.002		0.004		-0.004
		(0.369)		(0.835)		(-1.033)
Board Independence	-0.017	-0.023	0.018	0.026	-0.015	-0.030**
	(-1.022)	(-1.474)	(0.852)	(1.370)	(-1.026)	(-2.225)
Board Meeting	-0.010	-0.010	0.002	0.002	0.010*	0.009*
	(-1.540)	(-1.619)	(0.273)	(0.309)	(1.864)	(1.733)
Board Size	0.002	0.002	-0.041***	-0.042***	0.020***	0.021***
	(0.223)	(0.296)	(-4.114)	(-4.160)	(2.827)	(2.965)
Duality	0.012**	0.012**	-0.012*	-0.012*	0.004	0.004
	(2.111)	(2.024)	(-1.675)	(-1.667)	(0.884)	(0.776)
Leverage	-0.057***	-0.057***	0.006	0.006	0.037**	0.037**
	(-2.969)	(-2.993)	(0.257)	(0.257)	(2.297)	(2.273)
Firm Age	0.000	0.000	-0.001***	-0.001***	0.000***	0.000***
	(0.338)	(0.469)	(-4.646)	(-4.725)	(4.597)	(4.834)
Firm Size	-0.002	-0.002	0.015***	0.015***	-0.008***	-0.008***
	(-1.156)	(-1.034)	(7.569)	(7.586)	(-5.890)	(-5.785)
Sales Growth	-0.000	-0.000	0.000	0.000	-0.000	-0.000
	(-0.072)	(-0.078)	(1.101)	(1.083)	(-0.095)	(-0.071)
Market-to-Book Ratio	0.000***	0.000***	-0.000***	-0.000***	-0.000	-0.000
	(6.344)	(6.378)	(-7.069)	(-7.075)	(-1.031)	(-0.992)
ROA	0.204***	0.204***	-0.398***	-0.399***	-0.036**	-0.036**
	(11.373)	(11.365)	(-18.254)	(-18.276)	(-2.400)	(-2.353)
Return Volatility	-0.000***	-0.000***	0.000**	0.000**	-0.000	-0.000
	(-3.290)	(-3.275)	(2.255)	(2.259)	(-0.828)	(-0.818)
Big4 Auditor	0.007*	0.007*	-0.005	-0.005	-0.017***	-0.017***
	(1.851)	(1.859)	(-0.990)	(-1.006)	(-4.911)	(-4.876)
Intercept	0.079***	0.077***	-0.066**	-0.068**	-0.000	0.000
	(3.127)	(3.029)	(-2.144)	(-2.194)	(-0.013)	(0.006)
Industry FE	Yes	Yes	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes	Yes	Yes
Observations	4,964	4,964	4,964	4,964	4,964	4,964
R-squared	0.0981	0.0979	0.2172	0.2173	0.1394	0.1389

4.4.3.4 CEO-audit committee cultural similarity and earnings management

Thus far, we have examined the effects of cultural similarity between CEO and directors on earnings management by focusing on the entire board. In this section, we are interested in exploring the effects of cultural similarity on audit committee effectiveness in constraining earnings management. In general, the board assigns an audit committee to oversee the firm's financial reporting and audit processes by meeting regularly with the firm's external auditors, ensuring the accuracy of the firm's financial statement, and reviewing the internal accounting controls (Klein 2002).

Nevertheless, although such a committee is responsible for upholding the credibility of reported earnings, the appointment of an audit committee does not exempt the full board function in ensuring the credibility of financial reporting and the quality of reported earnings. Moreover, the findings of prior research on the roles and effectiveness of audit committees on earnings management are mixed. For instance, Beasley (1996) and Peasnell et al. (2005) show that there is no relationship between the audit committee and earnings management. However, other studies find audit committees reduce earnings management (e.g., Klein 2002; Xie et al. 2003; Bédard et al. 2004). Furthermore, Hwang and Kim (2012) suggest that, if a CEO has social ties with members of the audit committee, this increases earnings management.

Thus, motivated by the prior research, we further consider the implication of CEO-audit committee cultural similarity on earnings management. Specifically, we repeat our main analysis after redefining our variable of interest as the fraction of audit-committee members who share a similar culture to the CEO and denote it as *CEO-AC Cultural Similarity*. We re-estimate the regressions by focusing on the cultural similarity between the CEO and the members of the audit committee, *CEO-AC Cultural Similarity*.

Results in **Table 4.14** suggest that the coefficient on CEO-*AC Cultural Similarity* is not significant for any of the earnings management measures, indicating that there is no relationship between CEO-AC cultural similarity and earnings management. This also implies that CEO-AC cultural similarity has less incremental power than the CEO-board cultural similarity in explaining variations in earnings management. Thus, our findings highlight the significance of analysing the CEO's cultural ties with the board as a whole and not just the audit committee. As suggested by prior research

(DeFond et al. 2005; Krishnan and Visvanathan 2008; Krishnan et al. 2011), the effectiveness of an audit committee may be contingent on the corporate governance the firm has in place and its effectiveness may be weakened in practice by a dysfunctional board.

Table 4. 14: CEO-audit committee cultural similarity and earnings management

This table reports the OLS estimation results of accrual-based and real earnings management on measures of CEO-board cultural similarity, board characteristics, and firm characteristics for Malaysian non-financial listed firms in the sample period of 2009 to 2016. *CEO-AC Cultural Similarity* is the proportion of audit committee members that share similar ethnicity with the CEO. All other variables are defined in **Table 4.2**. Standard errors are clustered at the firm level and t-statistics are reported in parentheses. ***, **, * indicate statistical significance at the 1%, 5%, and 10% level, respectively.

	SDA	***AB_CFO***	***AB_PROD***	***AB_DIS***
	(1)	**(2)**	**(3)**	**(4)**
CEO-AC Cultural Similarity	0.000	0.000	-0.001	0.000
	(0.724)	(0.276)	(-1.319)	(0.078)
Board Independence	0.070***	-0.024	0.025	-0.026**
	(2.823)	(-1.534)	(1.311)	(-1.987)
Board Meeting	-0.021**	-0.011*	0.005	0.008
	(-2.022)	(-1.768)	(0.635)	(1.506)
Board Size	-0.001	0.002	-0.041***	0.020***
	(-0.068)	(0.213)	(-4.061)	(2.933)
Duality	-0.006	0.011*	-0.010	0.003
	(-0.595)	(1.952)	(-1.438)	(0.600)
Leverage	0.029	-0.058***	0.009	0.035**
	(0.947)	(-3.052)	(0.401)	(2.210)
Firm Age	-0.000	0.000	-0.001***	0.000***
	(-0.274)	(0.665)	(-5.646)	(5.560)
Firm Size	0.004	-0.002	0.014***	-0.008***
	(1.361)	(-0.988)	(7.340)	(-5.798)
Sales Growth	0.000	-0.000	0.000	-0.000
	(0.489)	(-0.072)	(1.091)	(-0.097)
Market-to-Book Ratio	-0.000***	0.000***	-0.000***	-0.000
	(-2.707)	(6.372)	(-7.149)	(-0.973)
ROA	0.297***	0.204***	-0.395***	-0.038**
	(8.179)	(11.340)	(-18.160)	(-2.513)
Return Volatility	0.002***	-0.000***	0.000**	-0.000
	(7.493)	(-3.284)	(2.323)	(-0.815)
Big4 Auditor	-0.003	0.008*	-0.006	-0.016***
	(-0.397)	(1.913)	(-1.317)	(-4.590)
Intercept	-0.054	0.077***	-0.056*	-0.003
	(-1.307)	(3.010)	(-1.793)	(-0.150)
Industry FE	Yes	Yes	Yes	Yes
Yeas FE	Yes	Yes	Yes	Yes
Observations	4,153	4,939	4,939	4,939
R-squared	0.0396	0.0974	0.2190	0.1407

4.5 Conclusion

To identify one of the potential causes of the negative valuation impact of CEO-board cultural similarity, we have explored the relationship between CEO-board cultural similarity and the quality of financial reporting as reflected in the practice of earnings management. The most important findings are highlighted:

First, we find that firms with a higher fraction of cultural similarity between the CEO and the board of directors are more likely to engage in income-increasing accrual-based earnings management. The results are robust to an endogeneity check, which uses the instrumental variable approach and an alternative measure of earnings management (i.e., real-earnings management) as a robustness test.

Second, the analysis finds that firms with a higher cultural similarity between the CEO and the board of directors are more likely to engage in income-increasing accrual-based earnings management as well as income-increasing real-earnings management, even after controlling for CEO power as proxied by CEO duality. Third, we find that boards are more effective at reducing earnings management when they are both formally and culturally independent.

Fourth, we also find that cultural similarity prevents independent directors from performing their monitoring role effectively. Finally, we find no evidence of a relationship between the CEO-audit committee cultural similarity and earnings management.

Overall, the findings from this chapter highlight that CEO-board cultural similarity impairs the board monitoring effectiveness and leads to weak internal control over financial reporting quality and process. This could be one of the potential sources of the negative valuation impact of cultural similarity that was evident in **Chapter 3**.

Now that we have established that CEO-board cultural similarity reduces the effectiveness of board monitoring and independence and financial reporting quality, the next chapter will discuss another potential cause of the negative evaluation impact of CEO-board cultural similarity by examining whether the cultural similarity between the CEO and other board members is associated with managerial entrenchment. Specifically, the next chapter will empirically investigate the association between CEO-board cultural similarity and involuntary turnover.

Chapter 5

CEO-Board Cultural Similarity and Involuntary Turnover

5.1 Introduction

In this chapter, we further investigate another potential cause of the negative valuation impact of CEO-board cultural similarity by examining whether the cultural similarity between the CEO and other board members is associated with managerial entrenchment as reflected in involuntary CEO turnover.

CEO turnover is an important corporate governance mechanism for disciplining managers and deterring them from any self-serving behaviour. Ideally, shareholders can rely on the board of directors, the primary internal monitor, to remove a non-performing CEO. In reality, however, board directors often fail to dismiss an ineffective CEO (Weisbach 1988; Huson et al. 2001; Goyal and Park 2002). Prior research attributes such a dysfunctional board to the presence of achieved social connections (i.e., prior employment, education, or club membership) between the CEO and other board members (e.g., Hwang and Kim 2009; Nguyen 2012). Nevertheless, there is limited evidence on the effect of salient ascribed connections such as cultural ties between CEO and other directors on governance outcomes.

In this study, we further examine the extent to which cultural ties between a CEO and board members affect monitoring effectiveness and managerial entrenchment. Just as 'similarity breeds connections' and 'birds of a feather flock together', the well-evidenced concepts from homophily theory suggest that people can be strongly connected through similarity in cultural background and identity (McPherson et al. 2001). While a stream of research has examined the impact of cultural similarities and distances on many aspects of corporate decision-making (Bryan et al. 2015; Shi and Tang 2015; Lim et al. 2016), the issue of whether CEO-board cultural similarity affects involuntary CEO turnover has been overlooked. Drawing from homophily and social

identity theory (Tajfel and Turner 1986; Turner 1987; McPherson et al. 2001), we postulate that cultural similarity motivates the CEO and directors to identify themselves into the same group, which can develop empathy, acceptance, and trust between them, which affects the board's monitoring and its oversight over the CEO. As a consequence, the cultural ties may reduce the directors' incentives to remove an underperforming CEO.

To test our hypothesis, we gather a large sample of publicly listed companies in Malaysia and focus on 2009-2016. CEO-board cultural similarity is measured by the fraction of the board of directors that share similar ethnicity with the CEO. Accordingly, we focus on involuntary CEO turnover to measure the firm's managerial entrenchment. Following prior research, we define turnover as involuntary if there is a CEO change between year t and t + 1 and the departing CEO is less than 60 years old (Coles et al. 2014; Balsam et al. 2017). Using a sample of 621 non-financial Malaysian firms over the period 2009-2016, we show that firms with a higher proportion of CEO-board cultural similarity (henceforth referred to as 'cultural similarity') are associated with lower involuntary turnover. We also find that cultural similarity mitigates turnover-performance sensitivity. This evidence suggests that cultural ties can insulate underperforming CEOs from dismissal and may, therefore, represent an important source of managerial entrenchment.

Further, our study also shows that the negative effect of CEO-board cultural similarity on involuntary turnover is robust to a variety of robustness tests. Next, we recognise that the relationship that we are examining may be endogenous and our empirical tests account for that. Our results suggest that cultural connections with board members protect underperforming CEOs from dismissal. Nevertheless, it is possible to argue that our results are driven by the possibility that the likelihoods of forced turnover and cultural similarity are jointly determined. Specifically, CEOs may choose to appoint individuals that share their cultural background, to reduce their risk of dismissal. While we can never entirely rule out the endogeneity problem, we conduct an endogeneity test to mitigate this concern. Specifically, we use the instrumental variables approach to show that the negative relationship between cultural similarity and the likelihood of involuntary CEO turnover is unlikely to be driven by endogeneity.

Motivated by prior evidence that CEOs who are also the chair of their boards possess superior power (Goyal and Park 2002), we also examine whether CEO duality affects the relationship between cultural similarity and involuntary turnover. We find that cultural similarity is significantly and negatively related to involuntary turnover only when the CEO is also the chair. Further analysis indicates that it is the cultural similarity between CEO and independent directors, rather than that between CEO and executive directors, that mitigates the involuntary CEO turnover, implying that cultural ties prevent conventionally independent directors from performing their monitoring duties.

Overall, our results indicate that CEO-board cultural similarity leads to managerial entrenchment, which could be one of the potential sources of the negative valuation impact of cultural similarity that was evident in **Chapter 3**.

Our study makes several contributions to the literature. First, we provide new insights into the literature on managerial discipline and entrenchment by showing that CEO characteristics, such as the CEO's cultural connections with other board members, represent an important source of managerial entrenchment. In particular, we show that CEO-board cultural similarity safeguards poor-performing managers from dismissal. Second, we add to the strand of literature on culture and corporate finance, which highlights the relevance of the country-level cultural distance to foreign investments and corporate decisions.[15] There is relatively little empirical work on how the cultural similarity between managers and other board members affects corporate decisions. We fill this void by providing the first empirical evidence on the impact of the CEO-board cultural ties on the effectiveness of board monitoring from the perspective of CEO turnover. We also contribute to the literature on the role of culture in the context of boards (e.g., Bryan et al. 2015; Frijns et al. 2016; Nguyen et al. 2018) by focusing on how the cultural similarity between CEO and other board members affects the effectiveness of board monitoring and the involuntary CEO turnover.

Finally, we complement the growing line of research on the impact of cultural similarity on corporate outcomes. Several studies focus mainly on the social reciprocity between CEO and other directors, showing that such reciprocity weakens

[15] Among these studies are Ahern et al. (2015), Bryan et al. (2015), Lim et al. (2016), Shi and Tang (2015), and Zheng et al. (2012).

the monitoring intensity of boards and reduces firm value (e.g., Hwang and Kim 2009; Fracassi and Tate 2012; Goergen et al. 2015; Lee et al. 2014). Another strand of literature indicates that socially dependent boards are associated with lower CEO turnover risk than their socially independent counterparts (Hwang and Kim 2009; Nguyen 2012; Kramarz and Thesmar 2013; Balsam et al. 2017). Unlike prior studies, we focus on how the cultural ties between the CEO and other board members affect the monitoring effectiveness of the board and CEO turnover probability.

The remainder of the chapter proceeds as follows. **Section 5.2** provides a brief review of the related literature and develops our hypothesis. **Section 5.3** describes our method and data. **Section 5.4** discusses our results and **Section 5.5** concludes.

5.2 Literature review and hypothesis development

5.2.1 Board monitoring and CEO turnover

Several studies have documented a significantly negative association between firm performance and CEO turnover (e.g., Coughlan and Schmidt 1985; Warner et al. 1988; Weisbach 1988). Others (e.g., Huson et al. 2004; Evans et al. 2014) find that a forced CEO turnover improves firm performance. Existing literature has also identified factors such as CEO duality, managerial ownership, social networks with controlling owners, managerial outside options, and takeover provisions that reduce the probability of CEOs being replaced (Goyal and Park 2002; Chen et al. 2013; Dikolli et al. 2014; Liu 2014).

Involuntary, or forced, CEO turnover is an important corporate governance event in disciplining managers and enhancing efficiency. According to Gibson (2003) and Macey (1998), an effective governance system should aim to eliminate and replace poorly performing managers. A resistance to replace those poorly performing managers might induce agency costs (Jensen and Ruback 1983) and exert adverse influences on a firm's investment, operating, and financing decisions (Huson et al. 2001). As a critical element of the internal governance mechanism, the board of directors is widely believed to play an important role in monitoring managers and removing underperforming CEOs. Whereas the pioneering studies on managerial

turnover find that the likelihood of CEO turnover decreases in relation to increased firm performance, later research suggests that the relationship between turnover and performance is weaker in poorly governed firms (DeFond and Park 1999; Huson et al. 2001; Goyal and Park 2002; Parrino et al. 2003). Most of this research focuses on the effectiveness of boards to discipline underperforming CEOs by terminating their employment contracts. For example, Goyal and Park (2002) suggest that turnover-performance sensitivity is weaker if the CEO and the chair's duties are vested in the same individual[16]. They argue that the lack of board independence results in less monitoring of top management and consequently affects the board's effectiveness in replacing the poorly performing managers.

Board independence has been embraced as a key characteristic of 'good' corporate governance. In fact, prior research suggests that board effectiveness can be hampered by a lack of independence between top management and other board members, resulting in a negative effect on firm performance (Fracassi and Tate 2012) and board monitoring (Adams and Ferreira 2007). Another strand of literature has shown that close or personal connections, such as prior employment, education, or membership of a similar organisation, between a CEO and other directors on a board reduce the effectiveness of board monitoring (e.g., Hwang and Kim 2009; Krishnan et al. 2011; Bruynseel and Cardinaels 2014). For example, Balsam et al. (2017), Hwang and Kim (2009), Kramarz and Thesmar (2013), and Nguyen (2012) find that CEOs receive greater compensation and enjoy lower turnover risks when working for firms with socially dependent boards. Complementing this literature, our study investigates the extent to which cultural/ethnic connections between CEO and other board members affect the effectiveness of board monitoring. Our argument is based on the premise that social connections tend to occur among individuals with similar attributes, particularly ethnicity (McPherson et al. 2001). Since ethnicity is a major predictor of culture that connects individuals (Desmet et al. 2017), the cultural similarity between CEO and board should serve as a key element of the CEO-board connections.

[16] Several studies have documented that CEO duality may jeopardise board independence and board effectiveness in monitoring top management. Among these studies are Jensen (1993) and Fama and Jensen (1983).

5.2.2 Hypothesis development

From an agency perspective, the board's key role is to protect shareholders' interests by ensuring that the CEO's actions and decisions are free from any self-serving behaviour. Thus, effective boards are responsible for monitoring managers' behaviour and removing non-performing CEOs. However, boards do not always fulfil their governance obligations (Huson et al. 2001; Goyal and Park 2002; Brunello et al. 2003; Coles et al. 2014), and close or personal connections, such as prior employment, education, or membership of similar organisations, between CEO and board members hamper the effectiveness of board monitoring and the board's ability to dismiss an ineffective CEO (Hwang and Kim 2009; Krishnan et al. 2011; Bruynseel and Cardinaels 2014).

Prior research documents that the CEO-board connections exert an adverse influence on the governance quality of firms. For instance, Krishnan et al. (2011) find that a CEO-board social network increases the likelihood of the CEO engaging in earnings management. Fracassi and Tate (2012) show that firms with more CEO-director ties engage in more value-destroying acquisitions. Others, such as Larcker et al. (2007), Hoitash (2011), and Hwang and Kim (2009), find that social ties hinder the quality of monitoring and increase CEO compensation. Deviating from prior literature, we examine the impact of CEO-board cultural ties on the propensity of boards to dismiss non-performing CEOs. As a critical element of the internal governance mechanism, the board of directors is widely believed to play an important role in monitoring managers and in removing underperforming CEOs. Nevertheless, the presence of a social or personal connection between the CEO and the board could hinder the effectiveness of the board to execute its responsibility properly. Prior studies indicate that socially dependent boards are associated with lower CEO turnover risk than their socially independent counterparts (Hwang and Kim 2009; Nguyen 2012; Kramarz and Thesmar 2013; Balsam et al. 2017). Nevertheless, these studies have focused on the social ties that developed from achieved social ties such as employment, club membership, and educational background.

An important attribute that has been overlooked by many prior studies is that common culture and identity can spur strong connections among individuals. According to McPherson et al. (2001), social connections tend to occur among individuals with

similar attributes, particularly in race and ethnicity. As ethnicity is deemed to be the core predictor of culture that connects individuals, we maintain that ethnic similarity between CEO and board could serve as an effective proxy for CEO-board cultural connections. The shared cultural background between the CEO and the board can enable empathy, acceptance, and trust to develop between them, which would impact the kind of monitoring and oversight the board exerts over the CEO. As a consequence, board members with cultural connections to the CEO may not execute their monitoring responsibility properly and may be reluctant to dismiss an underperforming CEO. Based on the above reasoning, we hypothesise that:

Hypothesis: *CEO-board cultural similarity is associated with a lower likelihood of involuntary turnover*.

5.3 Data, variables, and descriptive statistics

5.3.1 Data and sample selections

Our sample starts with all non-financial firms listed on the main market of Bursa Malaysia (previously known as Kuala Lumpur Stock Exchange) over the period 2009 to 2016. Finance-related service firms were excluded, as they are based on different regulations and are closely supervised by the Central Bank. The period 2009-2016 represents an era in which Malaysia's financial and economic conditions were relatively stable after the global financial crisis.[17] After excluding observations with incomplete data, our final sample consists of 3,011 firm-year observations from 621 unique firms. Financial and accounting data were retrieved from S&P Capital IQ and DataStream, while non-financial information and corporate governance data were manually collected from annual reports, retrieved from the Bursa Malaysia website (www.bursamalaysia.com) and Bloomberg. The detailed sample selection process is shown in **Table 5.1**.

Table 5. 1: Sample selection process

This table reports the sample selection process and resulting firm-year observations. We begin with all listed firms on Capital IQ from 2009 to 2016. After deleting observations in financial and regulated industries as well as observations with incomplete financial and governance data, we have 3,011 from 2009 to 2016

No		Number of observations
1	Total number of firm-year observations from 2009 to 2016	7,448
2	Observations in financial (SIC 6000-6999) and utilities industries (SIC 4900-4999)	(1,327)
3	Do not have two consecutive years of data, which necessary to identify CEO turnover	(1,021)
4	Observations with incomplete data (financial or corporate governance)	(2,089)
	Final sample	3,011
	No of unique firms	621

[17] The quality of data in the earlier period (i.e., the 1990s) is rather poor, making it difficult to produce reliable results. Furthermore, lack of corporate governance reforms and structures in earlier periods (Malaysia's Corporate Governance Code was first initiated in 2000) makes it difficult to draw inferences about the governance role of cultural similarity.

5.3.2 Variables

5.3.2.1 Involuntary CEO turnover

Following prior research, we define turnover as involuntary or forced if there is a CEO change between year t and t + 1 and the departing CEO is less than 60 years old (Coles et al. 2014; Balsam et al. 2017). We set up a variable for forced CEO turnover. The *CEO forced* turnover dummy equals one if there is a forced turnover, and zero otherwise. Of the sample of 308 CEO turnovers, 250 (81.17%) are involuntary. **Table 5.2** reports the distribution of these observations over the years 2009-2016.

Table 5. 2: CEO turnover by year from 2009 to 2016

This table reports the total number of firm-year observations and cases of CEO turnover and involuntary CEO turnover from 2009 to 2016.

Year	Number of observations	Number of turnovers	Involuntary turnover	Involuntary as a % of total turnovers
2009	704	32	27	84.37%
2010	710	40	37	92.50%
2011	726	39	31	79.50%
2012	737	36	31	86.11%
2013	747	46	37	80.43%
2014	754	43	28	65.11%
2015	760	43	35	81.39%
2016	761	29	24	82.75%
	5899	308	250	81.17%

5.3.2.2 Cultural similarity

The measurement of cultural similarity and the construction of our key variable of interest, the cultural similarity between CEO and other board directors (*Cultural Similarity*), were previously discussed in more detail in **Section 2.4.4.**

5.3.2.3 Control variables

We incorporate a set of variables that are known to affect involuntary CEO turnover in our regressions. Prior literature suggests that effective corporate governance provides better board monitoring, alleviates agency problems, and mitigates managerial entrenchment (e.g., Weisbach 1988; Dahya et al. 2002; Dahya et al. 2008; Hwang and Kim 2009). Thus, we account for such an effect by including *Board*

Independence, measured as a percentage of independent directors, and *Board Size*, measured as a natural logarithm of the number of directors on the board. We also control for CEO characteristics, such as duality (*CEO is Chair*), age (*CEO Age*), and tenure (*CEO Tenure*), that may affect involuntary turnover (Weisbach 1988; Shen and Canella 2002).

Firm-specific characteristics, such as a change in return on assets (*Return on Assets*), industry-adjusted stock returns (*Stock Returns*), industry-adjusted return on sales (*Return on Sales*), and the natural logarithm of sales growth (*Sales Growth*), market risk (*Return Volatility*) and *Firm Size*, measured as the natural logarithm of the firm's total assets, which are suggested to affect CEO turnover (Brickley 2003; Graham et al. 2005; Jenter and Lewellen 2021) are also accounted for in our regressions. Detailed variable definitions can be found in **Table 5.3**.

5.3.3 Descriptive statistics and correlation matrix

Table 5.4 presents the descriptive statistics of the variables used in our analysis. The mean of *Cultural Similarity* is 0.69, suggesting that the majority of the directors on the board share similar culture/ethnicity with the companies' CEO. The average *Board Size* is about 7 members and ranges from 3 to 22 members. The mean percentage of independent members on the board is 47%, with values ranging from 11% to 100%. Our data also indicate that the averages of the *CEO Tenure* and *CEO Age* are 9.1 and 53 years, respectively. It further shows that the dual leadership structure is not a common feature for Malaysian listed firms, as only 11% of the CEOs serve as board chairpersons.

As for the firm characteristics, the average *Firm Size* is 5.75 million MYR. The large variation in the *Return on Assets* indicates that Malaysian companies differ greatly in their profitability. In our sample, the averages of *Stock Returns*, *Return on Sales*, and *Sales Growth* are 15.44, -0.02, and 0.11 respectively. These statistics differ slightly from those of Gul et al. (2016) and Bhatt and Bhatt (2017), presumably because our sample contains more recently listed firms. The average monthly return volatility of 11.65% is consistent with that reported by Gul et al. (2016).

Table 5.5 exhibits the Pearson correlation coefficients for the regression variables. Most of the pairwise correlations among the independent variables are below 0.50, indicating that collinearity is unlikely to be a major problem in our analysis. To further

test the existence of multicollinearity, we also compute the variance inflation factor (VIF) for all independent variables. The highest VIF is only 1.41, which is far below the recommended threshold value of 10.00 for multiple regression models (Hair et al. 1998; Kennedy 1998), confirming that multicollinearity is not a serious concern in our study.

Table 5. 3: Variable definitions and data sources

Variable	Definition	Sources
Dependent variables		
Involuntary CEO Turnover	Equals one if a CEO change is involuntary, and zero otherwise. We categorise CEO change as involuntary by following Coles et al. (2014) and Balsam et al. (2017); if there is a CEO change between year t and t+1 and CEO is less than 60 years old	Bloomberg and annual report
Independent variables		
Cultural Similarity	The proportion of board directors that share similar culture/ethnicity with the CEO.	Bloomberg and annual report
Cultural Similarity-dummy	Equals one if *Cultural Similarity* is above the sample mean, and zero otherwise.	Bloomberg and annual report
Cultural Similarity-independent	The proportion of the board that consists of directors that share a similar cultural background with the CEO and are independent.	Bloomberg and annual report
Cultural Similarity-Executive	The proportion of the board that consists of directors that share a similar cultural background with the CEO and are executive/non-independent.	Bloomberg and annual report
Board characteristics		
Board Size	The number of directors on the board; log-transformed.	Annual report
Board Independence	The percentage of independent directors on board.	Annual report
CEO characteristics		
CEO Tenure	Number of years as the CEO.	Annual report
CEO is Chair	Equals one if the CEO is the chair of the board, and zero otherwise.	Annual report
CEO Age	The age of the current CEO.	Annual report
Firm characteristics		
Firm Size	The natural logarithm of total assets.	Capital IQ
Return Volatility	The standard deviation of monthly stock returns during a calendar year (in %).	DataStream
Return on Assets	Changes in return on assets, measured by operating income divided by the year-end book value of total assets; scaled and log-transformed.	Capital IQ
Return on Sales	Net income/sales; industry adjusted.	Capital IQ
Stock Return	Annual stock return; the 12-month stock return during the fiscal year; industry adjusted.	Capital IQ
Sales Growth	The annual growth rate of the firm's total assets, log-transformed.	Capital IQ

Table 5. 4: Summary statistics

This table reports summary statistics for CEO-board cultural similarity, firm performance, and control variables for a sample containing the non-financial firms listed in Bursa Malaysia. The final sample contains unbalanced panel data for 620 Malaysian firms for the period between 2009 and 2016. All variables are as defined in **Table 5.3.**

Variable	Obs.	Mean	Stdev.	Min.	0.25	Median	0.75	Max.
Cultural Similarity	5670	0.69	0.23	0.00	0.57	0.75	0.83	1.00
Cultural Similarity-Dummy	5670	0.98	0.14	0.00	1.00	1.00	1.00	1.00
Return on Assets	5,685	0.05	0.11	-0.88	0.01	0.05	0.10	0.96
Stock Return	5223	15.44	59.36	-61.36	-14.28	3.44	29.82	228.57
Return on Sales	5726	-0.02	1.18	-1.88	0.01	0.07	0.14	0.54
Sales Growth	5590	0.11	1.46	-0.73	-0.09	0.03	0.16	2.12
Return Volatility	5398	11.65	13.78	0.00	5.97	9.11	13.73	458.76
Firm Size	5631	5.75	1.65	-5.81	4.63	5.58	6.66	11.84
Board Size	5,641	7.33	1.94	3.00	6.00	7.00	8.00	22.00
Board Independence	5,643	0.47	0.13	0.11	0.38	0.44	0.57	1.00
CEO Tenure	5869	9.10	7.11	0.00	4.00	7.00	12.00	46.00
CEO is Chair	5800	0.11	0.31	0.00	0.00	0.00	0.00	1.00
CEO Age	5867	53.06	9.08	24.00	47.00	53.00	59.00	83.00

Table 5. 5: Correlation matrix

This table reports the correlation matrix among the main variables used in our econometric analyses. Correlation coefficients significant at the 1% level or better are in bold. Refer to **Table 5.3** for detailed variable description.

	Variables	**1**	**2**	**3**	**4**	**5**	**6**	**7**	**8**	**9**	**10**	**11**	**12**	**13**
1	*Cultural Similarity*	1												
2	*Cultural Similarity-dummy*	**0.781**	1											
3	*Return on Assets*	0.002	0.013	1										
4	*Stock Return*	-0.001	0.003	0.006	1									
5	*Return on Sales*	-0.020	-0.019	-0.005	-0.010	1								
6	*Sales Growth*	-0.005	-0.014	0.006	0.026	-0.006	1							
7	*Return Volatility*	0.008	0.020	0.001	**0.128**	-0.000	0.009	1						
8	*Firm Size*	**-0.129**	**-0.155**	**0.078**	**0.063**	-0.009	0.000	**-0.190**	1					
9	*Board Size*	-0.012	**-0.070**	-0.024	**0.035**	-0.007	0.000	**-0.105**	**0.386**	1				
10	*Board Independence*	**-0.069**	-0.019	0.023	-0.017	-0.014	0.011	**0.057**	**-0.069**	**-0.371**	1			
11	*CEO Tenure*	**0.055**	**0.032**	0.001	**0.050**	0.006	**-0.030**	**-0.058**	**0.075**	**0.089**	**-0.067**	1		
12	*CEO is Chair*	**0.108**	**0.075**	0.007	0.001	-0.010	-0.002	0.017	**-0.058**	**-0.080**	0.012	**0.075**	1	
13	*CEO Age*	0.005	-0.011	0.040	**0.036**	-0.003	**-0.039**	-0.097	0.144	**0.071**	**-0.039**	**0.396**	**0.115**	1

5.4 Empirical results

5.4.1 Cultural similarity and involuntary CEO turnover

We hypothesise that the CEO-board cultural similarity is associated with the lower likelihood of involuntary turnover. To test this, we estimate the following logit model*:*

$$Forced_{it} = a_0 + a_1 Cultural\ Similarity_{it-1} + a_5 Board\ characteristics_{it-1} + a_6 CEO\ characteristics_{it-1} + a_7 Firm\ characteristics_{it-1} + Year\ and\ Industy\ Fixed\ Effects + \varepsilon_{it} \quad (\mathbf{5.1})$$

where the subscripts *i* and *t* represent the firm and year, respectively; *Forced* is a dummy variable that equals one if involuntary turnover occurred in the firm year; *Cultural Similarity* is the proportion of board directors that share similar ethnicity; board characteristics variables represent *Board Independence* and *Board Size*; CEO characteristics variables consist of *CEO Tenure*, *CEO is Chair*, and *CEO Age*; firm characteristics variables comprise *Return on Assets*, *Stock Returns*, *Return on Sales*, *Sales Growth*, *Return Volatility*, and *Firm Size*; two-digit SIC *Industry dummies* are included to account for the industry fixed effect and *Year dummies* are added to account for the year fixed effect. We lag all explanatory variables on the right-hand side by one year to alleviate potential endogeneity concerns (Faleye et al. 2014). In computing the statistical significance of the estimation, we cluster standard errors by the firm.

Table 5.6 exhibits the impact of CEO-board cultural similarity on involuntary CEO turnover. We begin the analyses by regressing *Forced/Involuntary CEO Turnover* on *Cultural Similarity*. In column (1), the coefficient on *Cultural Similarity*, as the only explanatory variable, is negative (b=-0.873), and significant at the 1% level. Column (2) shows similar results after firm characteristics are introduced (b=-0.120, p<.01). Column (3) presents the test results after controlling for both board and firm characteristics. The inclusion of the two groups of control variables also does not alter the sign or the significance of the *Cultural Similarity* (b=-0.124, p <.01). Column (4) shows similar results after controlling for the firm, board, and CEO characteristics. Consistent with our hypothesis, the coefficient on the *Cultural Similarity* is negative

and statistically significant (b=-1.055, p <.01), indicating that CEO-board cultural similarity reduces the involuntary CEO turnover rate, which supports our **hypothesis.**

In economic terms, the use of the coefficient on *Cultural Similarity* to compute the predicted probability, when all the variables are set at their mean values, indicates that the probability of the CEO being forced out when firms employ at least one director with similar cultural background to the CEO is 0.04%. Overall, our results show that the presence of CEO-board cultural similarity reduces the probability of involuntary turnover. This evidence suggests that, in addition to the adverse effect of social networks on CEO turnover (Hwang and Kim 2009; Nguyen 2012; Balsam et al. 2017), 'other type of connections', namely the cultural similarity between CEO and board members, also weaken board independence and decrease the board's willingness to discipline the CEO.

The results of the control variables are generally consistent with prior literature. Specifically, in line with the previous research (Goyal and Park 2002; Hermalin and Weisbach 2003; Dikolli et al. 2014), we find that the coefficient on *CEO Tenure* is negative and significant at the 1% level, implying that longer-tenured CEOs are less likely to be forced out. Consistent with Core et al. (1999) and Balsam et al. (2017), we also find that the coefficient on *CEO Age* is negative and significant at the 5% level, indicating that older directors to be negatively associated with forced turnover. We also find that the coefficients on both *Board Size* and *Board Independence* are positive and significant, indicating that firms with larger board and higher proportion of independent directors are associated with increased involuntary turnover. Finally, the results also show that the coefficient on *Return Volatility* is positive and significant at 10% level, implying that firms with higher stock return volatility are positively associated with forced turnover, which is in line with Balsam et al. (2017) and Hazarika et al. (2012).

Table 5. 6: CEO-board cultural similarity and involuntary CEO turnover

This table reports the coefficients estimated in the logit CEO turnover models. *Involuntary CEO Turnover* is a dummy variable that equals one if the CEO is forced out, and zero otherwise. *Cultural Similarity* is the proportion of board directors that share similar ethnicity with the CEO. All other variables are defined in **Table 5.3**. Standard errors are clustered at the firm level and t-statistics are reported in parentheses. ***, **, * denote statistical significance at the 1%, 5%, and 10% level, respectively.

	Involuntary CEO Turnover			
	(1)	**(2)**	**(3)**	**(4)**
Cultural Similarity	-0.873**	-0.120***	-0.124***	-1.055***
	(-2.553)	(-2.928)	(-2.885)	(-2.588)
Board Size			1.233***	1.206***
			(2.728)	(2.747)
Board Independence			2.056**	1.770**
			(2.461)	(2.179)
CEO Tenure				-0.064***
				(-3.349)
CEO is Chair				-0.542
				(-1.347)
CEO Age				-0.024**
				(-2.440)
Return on Assets		0.000	0.000	-0.000
		(0.152)	(0.107)	(-0.103)
Stock Return		-0.028	0.044	0.069
		(-0.168)	(0.270)	(0.422)
Return on Sales		0.000	-0.000	0.000
		(0.097)	(-0.118)	(0.095)
Sales Growth		7.443**	-26.439	-26.865
		(2.007)	(-1.254)	(-1.333)
Return Volatility		0.007	0.007	0.009*
		(1.506)	(1.571)	(1.846)
Firm Size		-0.011	-0.059	-0.027
		(-0.148)	(-0.754)	(-0.361)
Constant	-2.370***	-36.618**	115.926	119.228
	(-4.562)	(-2.149)	(1.192)	(1.283)
Year FE	Yes	Yes	Yes	Yes
Industry FE	Yes	Yes	Yes	Yes
Observations	4,510	3,063	3,015	3,011
Pseudo R2	0.0438	0.0489	0.059	0.084
Model significance				
Likelihood ratio chi-square	74.68	53.81	64.49	91.41
p-value	0.008	0.004	0.068	0.000

5.4.2 Robustness checks

After presenting the baseline evidence, we next verify the robustness of our main results to alternative variable definitions, alternative model specifications, and endogeneity concerns.

5.4.2.1 Alternative measurements and specifications

We subject the negative effect of CEO-board cultural similarity on the turnover probability to other robustness checks. **Table 5.7** reports the coefficients of our variable of interest, C*ultural Similarity*, obtained from various alternative measurements and specifications. Row (0) shows the results from our baseline specifications in **Table 5.6** for comparison. First, following prior research (Liu 2014), we use the natural log of Tobin's Q, measured as the book value of total assets minus the book value of equity plus the market value of equity, all divided by the book value of total assets, instead of stock returns, as a measure of firm performance. As row (1) shows, we continue to find a significantly negative relation between CEO-board cultural similarity and involuntary turnover.

Next, we use the natural log of total revenue, defined as the book value of total revenue, instead of the natural log of total assets, as a proxy for firm size. We again find a consistently negative relation between CEO-board cultural similarity and involuntary turnover (see row (2)).

The lack of public disclosure of turnover events (Gibson 2003; You and Du 2012) makes it difficult for researchers to distinguish between forced and voluntary turnovers. Thus, for robustness purposes, we also use a dummy variable, namely *All CEO Turnover*, to capture CEO turnovers for any possible causes (see, e.g., Firth et al. 2006; You and Du 2012). As shown in row (3), our result continues to hold when we use *All CEO Turnover* as the dependent variable in our baseline regressions.

Next, following Goyal and Park (2002) and Liu (2014), we also examine the robustness of our main findings to different classifications of retirement age. Age 64 is defined as an alternative retirement cut-off, instead of age 60. As shown in row (4), we find that the main results remain unchanged.

Following Goyal and Park (2002), we further test the robustness of our main findings by including the natural log of sales as a control variable. The results, shown in row (5), are qualitatively similar to those reported in **Table 5.6**.

Finally, row (6) confirms the validity of our results after excluding utility firms, which are heavily regulated, from our estimation. In sum, the negative effect of CEO-board cultural similarity on involuntary turnover is robust to a variety of robustness tests.

Table 5. 7: Robustness tests

This table reports the coefficient of our variable of interest, CEO-board cultural similarity (*Cultural Similarity*), from alternative specifications of the regressions. The main specification, shown in row (0), is the main regression on the full sample with the complete set of controls, as shown in column (4) of **Table 5.6**. Standard errors are clustered at the firm level and t-statistics are reported in parentheses. ***, **, * indicate significance at the 1%, 5% and 10% level, respectively.

		Cultural similarity			
		Coef.	***t-value***	***S.E***	***Obs.***
(0)	Main specification	-1.055***	-2.59	0.407	3,011
(1)	Tobin's Q as alternative performance measure, in place of stock returns	-0.734*	-1.77	0.416	3,129
(2)	Total revenue as alternative measures of firm size, in place of total assets	-1.018**	-2.53	0.401	3,00
(3)	All CEO turnover as the dependent variable	-0.876**	-2.46	0.356	3,211
(4)	Age 64 is used as an alternative retirement cut-off, instead of age 60	-0.735***	-2.97	0.422	3,012
(5)	Controlling for natural log of sales	-1.070***	-2.60	0.412	3,007
(6)	Excluding utility companies and regulated companies	-1.168**	-2.49	0.469	2,503

5.4.3 Endogeneity test

Our results suggest that cultural connections with board members protect underperforming CEOs from dismissal. Nevertheless, it is possible to argue that our results are driven by the possibility that the likelihoods of forced turnover and cultural similarity are jointly determined. Specifically, CEOs may choose to appoint individuals that share their cultural background, to reduce their risk of dismissal. While we can never entirely rule out the endogeneity problem, we conduct an endogeneity test to mitigate this concern.

5.4.3.1 Instrumental variable method

To alleviate endogeneity concerns, we use the two-stage least squares (2SLS) instrumental variable approach. Particularly, we employ an instrument that is unlikely to exert an effect on involuntary CEO turnover but should have an indirect relationship through its effects on CEO-board cultural similarity as well as work better in Malaysia context. The instrument we use in our study is a dummy variable for whether a firm is

headquartered outside of a large metropolitan city. One of the motivations deciding this instrument is that we expect firms headquartered in the small towns or outside of a large metropolitan area to be less culturally diverse than firms headquartered in larger city. This argument is consistent with Frijns et al. (2016) and Masulis et al. (2012) concerning their instruments which are mainly focused on the location of firms' headquarters as their instruments of board heterogeneity or cultural diversity.

We report the first-stage regression results in column (1) of **Table 5.8**, where we regress cultural similarity on the instrument and all the previously used controls. As expected, we find that instrumental variable is significantly positively associated with *Cultural Similarity*, confirming the validity of our instrument. In the second stage, we run a probit regression of involuntary CEO turnover on the predicted values of CEO-board cultural similarity from the first stage and all the control variables.

In column (2) of **Table 5.8**, we report the results of the second-stage regressions for *Involuntary CEO Turnover*. We find that the predicted *Cultural Similarity* estimated from the first regression is significant and negatively associated with *Involuntary CEO Turnover*, indicating that CEO-board cultural similarity reduces the probability of forced turnover. These results corroborate those reported in **Table 5.6**, implying that the negative association between cultural similarity and involuntary turnover is unlikely to be driven by endogeneity.

Table 5. 8: Endogeneity test: Instrumental variables estimation

This table reports instrumental variables regression estimation results. Column (1) reports the first-stage results of the 2SLS regressions with *Cultural Similarity* as the dependent variable. *Involuntary CEO Turnover* is a dummy variable that equals one if the CEO is forced out, and zero otherwise. The *Cultural Similarity* is the proportion of board directors that share similar ethnicity with the *CEO*. *Malaysia Small Town* is a dummy variable which equals one if a firm is headquartered outside of a large metropolitan area and zero, otherwise. Column (2) reports the second-stage results from 2SLS regressions for *Involuntary CEO Turnover*, respectively. All other variables are defined in **Table 5.3**. Standard errors are clustered at the firm level and t-statistics are reported in parentheses. ***, **, * indicate significance at the 1%, 5% and 10% level, respectively

	First stage	**Second stage**
	Cultural Similarity	***Involuntary CEO Turnover***
	(1)	**(2)**
Malaysia Small Town	0.059***	
	(6.875)	
Cultural Similarity		-3.539***
		(-6.587)
Board Size	0.028	0.479***
	(1.566)	(3.099)
Board Independence	-0.108***	0.200
	(-3.245)	(0.614)
CEO Tenure	0.002***	-0.013*
	(3.524)	(-1.656)
CEO is Chair	0.056***	0.018
	(4.445)	(0.125)
CEO Age	0.000	-0.008*
	(0.284)	(-1.884)
Return on Assets	-0.000	-0.001
	(-0.607)	(-0.299)
Stock Return	0.006	0.027
	(0.695)	(0.419)
Return on Sales	-0.000*	-0.000
	(-1.869)	(-0.761)
Sales Growth	0.006	-7.166
	(0.695)	(-1.054)
Return Volatility	-0.001**	0.000
	(-2.273)	(0.118)
Firm Size	-0.021***	-0.083***
	(-7.687)	(-3.651)
Intercept	0.708	34.067
	(0.362)	(1.094)
Industry FE	Yes	Yes
Year FE	Yes	Yes
Observations	3,427	3,427
Wald test of exogeneity (/athrho = 0): chi2(1) =10.59 Prob> chi2 = 0.001		

5.4.3.2 Propensity Score Matching

We also employ a matching approach and apply propensity score matching techniques to mitigate concerns relating to self-selection (Rosenbaum and Rubin 1983; Shipman et al. 2017) and 'sample selection bias' that is triggered by observable factors (Dehejia and Wahba 2002). For instance, CEOs with high demographic similarity to directors are more prone to appoint similar directors (e.g., directors who share the same ethnicity) (Westphal and Zajac 1995) which affects the firm value.

We compare the firm value in firms with high cultural similarity (i.e., treatment firms) and a sample of control firms with low cultural similarity (i.e., control firms). We define the treatment firms as firms with an above-sample mean fraction of CEO-board cultural similarity and control firms as firms with a below-sample-mean fraction of CEO-board cultural similarity.

The propensity score matching method proceeds in two steps. First, we estimate a probit[18] model using the full sample to compute the probability (i.e., the propensity score) that a firm with a set of firm-level characteristics is run by the treatment firms. We use the same controls as those included in the baseline regression. The probit regression results are reported in column (1) in Panel A of **Table 5.9**. We find that firms with high cultural similarity are smaller, younger, more leveraged, and have lesser return on sales than their counterparts with low cultural similarity.

To ensure that firms in the treatment sample and control sample are comparable, we employ the nearest neighbour approach. Specifically, each firm with high cultural similarity is matched to a firm with a low cultural similarity that has the closest propensity score. In our matching, we require the maximum difference between the propensity scores of the firm with high and that with low cultural similarity to not exceed 0.1% in absolute value.

Next, we employ two diagnostic analyses to verify that firms in the treatment and control groups are indistinguishable in terms of observable characteristics. First, we re-estimate the probit model for the post-match sample. Column (2) in Panel A shows that all of the estimated coefficients are statistically insignificant, implying the absence

[18] We also use a logit model in the first step as an alternative test and the results are qualitatively similar.

of any distinguishable trends in firm value between the two groups. In addition, the estimated coefficients in column (2) are smaller in magnitude than those in column (1), signifying that the decrease in statistical significance is not simply driven by reduced sample size. Lastly, **Table 5.9** shows a decrease in pseudo-R-squared from 0.026 for the pre-match sample to 0.002 for the post-match sample. This implies that propensity score matching eliminates all observable differences other than those related to cultural similarity.

Second, we examine the differences for each observable characteristic between the treatment firms and the matched control firms. All univariate difference tests in Panel B of **Table 5.9** are statistically insignificant, indicating that the differences in firm value between the treatment and control groups are only due to the presence of cultural similarity.

Panel C of **Table 5.9** presents the propensity score matching estimates. The results indicate that there are significant differences, at the 1% level, in firm value between firms with high and those with low cultural similarity.

Finally, we re-estimate the baseline model by using treatment and matched control sample and reports the result in Panel D of **Table 5.9**. The results show that the coefficient on *Cultural Similarity* is significantly negative in all specification, suggesting a positive association between cultural similarity and involuntary CEO turnover. Thus, the propensity score matching results are consistent with those in the baseline specification, implying that our main findings are unlikely to be influenced by omitted variables related to nonlinear forms of our control variables.

Table 5. 9: Propensity score matching estimates

This table reports the propensity score matching estimation results. Panel A reports estimates from the probit model used to estimate propensity scores. The dependent variable is a dummy variable that equals one for firms with high *Cultural Similarity*, and zero otherwise. We define a firm with high CEO-board cultural similarity (treatment firms) if it has an above-sample mean fraction of CEO-board cultural similarity and a firm with low CEO-board cultural similarity (control firms) if it has below-sample-mean fraction of CEO-board cultural similarity. All independent variables are defined in **Table 5.3**. Industry dummies are constructed based on the two-digit SIC code classification. Panel B reports the univariate comparisons of firm characteristics and board characteristics between treatment group and control group. Panel C reports the average treatments estimates. Panel D reports the regression results using PSM procedure. ***, **, and * indicate significance at the 1%, 5%, and 10% level, respectively.

Panel A: Pre-match propensity score regression and post-match diagnostic regression

	High Cultural Similarity Dummy	
	(1)	**(2)**
	Pre-Match	**Post-Match**
Board Size	-0.162	-0.203
	(-1.609)	(-1.023)
Board Independence	-0.396**	-0.508
	(-2.118)	(-2.032)
Return on Assets	-0.003	0.002
	(-1.416)	(0.849)
Stock Return	0.045	0.003
	(0.971)	(0.063)
Sales Growth	-0.484	1.545
	(-0.196)	(0.515)
Return on Sales	-0.000**	-0.000
	(-2.272)	(-1.603)
Return volatility	-0.005**	-0.002
	(-2.241)	(-0.821)
Firm size	-0.131***	-0.105
	(-8.617)	(-1.035)
CEO tenure	0.008**	0.007
	(2.343)	(1.561)
CEO age	0.005*	0.006
	(1.781)	(0.621)
Duality	0.138*	-0.003
	(1.916)	(-0.042)
Intercept	3.009	-6.228
	(0.265)	(-0.451)
Observations	3,427	3,302
Pseudo R^2	0.026	0.017
Industry FE	Yes	Yes
Year FE	Yes	Yes

Panel B: Differences in the firm and board characteristics

	Firm-year obs. with high CEO-board cultural similarity	Firm-year obs. with low CEO-board cultural similarity	Difference	*t*-stat
	(N=1,649)	(N=1.649)		
Board Size	1.949	1.9816	-0.0326	-1.54
Board Independence	0.46625	0.4736	-0.00735	-1.64
Return on Assets	9719.7	9754.8	-35.1	-0.01
Stock Return	4.5224	4.5259	-0.0035	-0.23
Sales Growth	4.6058	4.6064	-0.0006	-0.90
Return on Sales	-17.079	34.317	-51.396	-1.46
Return volatility	10.226	10.363	-0.137	-0.44
Firm size	5.7335	6.1436	-0.4101	-1.01
CEO tenure	10.356	9.8062	0.5498	0.25
CEO age	54.499	53.882	0.617	1.23
Duality	0.09509	0.08298	0.01211	1.22

Panel C: Propensity score matching estimator

Variables	Firm-year obs. with high CEO-board cultural similarity	Firm-year obs. with low CEO-board cultural similarity	Difference	T-stat
CEO forced	0.03290	0.0436	-0.0107***	-1.62
ATT	0.03452	0.0436	-0.0090***	-3.69

Panel D: The regression results using PSM procedure

	Involuntary CEO Turnover			
	(1)	**(2)**	**(3)**	**(4)**
Cultural Similarity	-1.057***	-1.056***	-1.061***	-0.825***
	(-2.712)	(-2.752)	(-2.638)	(-2.891)
Board Size			1.400***	-0.825**
			(3.166)	(-2.091)
Board Independence			2.301***	1.302***
			(3.231)	(3.040)
CEO Tenure				-0.078***
				(-3.702)
CEO is Chair				-0.699
				(-1.503)
CEO Age				-0.025***

				(-3.029)
Return on Assets		-0.001	-0.001	-0.002
		(-0.246)	(-0.438)	(-0.840)
Stock Return		0.037	0.002	0.029
		(0.203)	(0.013)	(0.166)
Return on Sales		-0.000	-0.000	-0.000
		(-0.331)	(-0.306)	(-0.002)
Sales Growth		-14.429	-16.276	-18.620
		(-0.814)	(-0.874)	(-1.079)
Return Volatility		0.007*	0.007*	0.009**
		(1.696)	(1.790)	(2.182)
Firm Size		-0.003	-0.071	-0.038
		(-0.039)	(-1.016)	(-0.568)
Constant	-2.504***	63.723	68.908	81.557
	(-9.572)	(0.780)	(0.803)	(1.025)
Year FE	Yes	Yes	Yes	Yes
Industry FE	Yes	Yes	Yes	Yes
Observations	3,298	3,298	3,298	3,298
Pseudo R2	0.007	0.009	0.002	0.059

5.4.3.3 Heckman selection model

A firm's decision to appoint a CEO with higher cultural ties with board of directors may be non-random and this may cause a self-selection bias. Thus, to address this concern, we conduct the Heckman two-step sample selection model as robustness check. In the first stage model, we compute the inverse Mills ratio from a probit model that captures the determinants of firms appointing CEO with similar cultural ties with board of directors. In particular, this probit model controls for a dummy variable (*Malaysia Small Town*) for whether a firm is headquartered outside of a large town in Malaysia. The motivation to use this exogenous variable is that we assume firms headquartered in these areas are to be less culturally diverse than firms headquartered in large towns (Anderson et al. 2011; Frijns et al. 2016). Furthermore, Heckman's estimator requires exogenous variable that is correlated with a firm's propensity to appoint CEO with similar cultural background with board of directors, but not with involuntary CEO turnover. Thus, the *Malaysia Small Town* is likely to be an important factor for a firm to appoint CEO that has higher cultural similarity with board of directors.

We also control for *Board Size, Board Independence, CEO Tenure, CEO is Chair, CEO Age, Return on Assets, Stock Returns, Return on Sales, Sales Growth, Return Volatility* and *Firm Size.* In the second stage, we include the inverse Mills ratio which is generated from first stage into the regression model as an additional control variable to control for the potential sample selection bias.

The results of the first-step regression in Column (1) of **Table 5.10** show that *Malaysia Small Town*. *CEO Tenure, CEO is Chair* have significant and positive impacts on the CEO-board cultural similarity, whereas *Board Independence, Firm Size, Return on Sales* and *Return Volatility* have significantly negative impacts.

The results of the second-step regression in Column (2) of **Table 5.10** show that the coefficient on *Cultural Similarity* is negative and insignificant. The coefficient on *Inverse Mills Ratio* is positive and insignificant.

Overall, our reported findings in **Table 5.10** are not qualitatively similar to our results reported under the main analysis and hence implying that our results reported under the main analysis do appear to be driven sample selection bias. Nevertheless, previous endogeneity tests show that our results are not driven by endogeneity and sample selection bias.

Table 5. 10: Heckman two-stage analysis

This table reports the regression results of Heckman model. The first step is a probit model with a binary cultural similarity dummy. *Dummy Cultural Similarity* equals one if the firm has an above-sample mean fraction of CEO-board cultural similarity and zero, otherwise. *Malaysia Small Town* is an exogenous variable, which equals one if the firm is headquartered in small towns and zero, otherwise. The second stage is ordinary least square regression of the impact of CEO-board cultural similarity on firm value. *Inverse Mills Ratio* is generated from the first step and included in the second step of this model. All other variables are defined in **Table 5.3**. Standard errors are clustered at the firm level and t-statistics are reported in parentheses. ***, **, * denote statistical significance at the 1%, 5%, and 10% level, respectively.

	First-step regression	Second-step regression
	Dummy Cultural similarity	***Involuntary CEO Turnover***
Cultural Similarity		-0.020
		(-0.664)
Malaysia Small Town	0.116**	
	(2.521)	
Board Size	0.159	0.058***
	(1.560)	(2.762)
Board Independence	-0.539***	0.086
	(-2.865)	(1.610)
CEO Tenure	0.008**	-0.001
	(2.217)	(-1.144)
CEO is Chair	0.239***	0.002
	(3.237)	(0.122)
CEO Age	0.004	-0.001
	(1.456)	(-0.987)
Return on Assets	-0.003	-0.000
	(-1.345)	(-0.355)
Stock Returns	0.004	0.004
	(0.090)	(0.463)
Return on Sales	-0.000*	-0.000
	(-1.731)	(-0.207)
Sales Growth	1.384	-0.089
	(0.582)	(-0.187)
Return Volatility	-0.004*	-0.000
	(-1.779)	(-0.848)
Firm Size	-0.103***	-0.011
	(-6.765)	(-1.336)
Inverse Mills Ratio		0.085
		(0.719)
Intercept	-5.974	0.336
	(-0.545)	(0.151)
Industry FE	Yes	Yes
Year FE	Yes	Yes
Observations	3,428	3,428
Pseudo R2	0.025	
Adjusted R2		0.086

5.4.4 Cultural similarity and turnover-performance sensitivity

Several studies document an inverse relationship between CEO turnover and firm performance (Coughlan and Schmidt 1985; Warner et al. 1988; Weisbach 1988), and most of the studies focus on firm performance as the core determinant of CEO turnover. However, agency and behavioural perspectives suggest that CEOs can take advantage of their social ties with the board of directors to protect themselves from dismissal (Hwang and Kim 2009; Nguyen 2012; Kramarz and Thesmar 2013; Balsam et al. 2017).

Hence, based on these perspectives, we argue that CEOs who share similar cultures with other board members are more likely to become entrenched in their positions and less likely to be monitored effectively by the board. Given that cultural ties with directors may facilitate bond, empathy, and trust between them, these CEOs are thus less likely to be replaced when they miss performance targets. Specifically, we expect that CEO-board cultural similarity is associated with lower turnover performance sensitivity. Given the inverse relationship between firm performance and involuntary CEO turnover, a positive coefficient would imply a lower sensitivity for firms with stronger CEO-board cultural similarity relative to those with no or weaker CEO-board cultural similarity.

We estimate equation model (**5.1**) by adding interactions between performance measures (*Stock Return, Return on Assets, Return on Sales* and *Sales Growth)* and *Cultural Similarity.* **Table 5.11** reports the results. Column (1) reports the results based on *Stock Returns* as the performance measure. Note that the estimated coefficient on the *Cultural Similarity Dummy* is consistently negative, implying that cultural similarity reduces the likelihood of involuntary CEO turnover. In addition, the estimated coefficient on the interaction between *Cultural Similarity Dummy* and *Stock Return* is positive (b=0.695) and significant at the 5% level, implying that cultural similarity reduces the sensitivity of involuntary CEO turnover to firm performance. Thus, CEOs seem to take advantage of their cultural ties with the board to protect themselves against the risk of dismissal in the case of poor performance and in times of distress. This finding adds the previous evidence on the impact of personal connections and social networks between directors on the governance quality of firms

(Westphal and Khanna 2003; Hwang and Kim 2009; Balsam et al. 2017) by identifying that cultural similarity exerts a negative influence on the effectiveness of board monitoring and involuntary CEO turnover.

Column (2) of **Table 5.11** shows that, when the *Return on Assets* is used as the performance measure, the results are similar to those of column (1). In addition, the estimated coefficient on the interaction between *Cultural Similarity Dummy* and *Return on Assets* is positive (b=0.017) and significant at the 5% level. The results remain qualitatively unchanged in columns (3) and (4), when we use *Return on Sales* and *Sales Growth* as the performance measures, respectively, although the significance of the interaction terms for both logit regressions is lower (at the 10% level). In addition, we also find that the estimated coefficient on *Sales Growth* is negative and significant at 5%, indicating that poor firm performance significantly increases the likelihood of involuntary CEO turnover. Overall, our results support our argument, which predicts that CEO-board cultural similarity is associated with lower turnover performance sensitivity.

The estimated coefficients on the control variables in **Table 5.11** are generally as expected. The coefficient on *CEO Tenure* is negative and significant at the 1% level in all model specifications, implying that the CEO turnover is less likely when CEOs have longer tenure. The coefficient on *CEO Age* is negative and significant in all four logit regressions, indicating that older directors are negatively associated with forced turnover. We also find that the coefficients on both *Board Size* and *Board Independence* are positive and significant across the logit regressions, indicating that firms with larger board and higher proportion of independent directors are associated with increased involuntary turnover. Next, the coefficient on *Return Volatility* is positive and significant at the 5% level in the first and fourth logit regressions, and positive and significant at the 10% level in the second and third logit regressions, implying that firms with higher stock return volatility are positively associated with forced turnover which is consistent with Balsam et al. (2017) and Hazarika et al. (2012).

Table 5. 11: Cultural similarity and turnover-performance sensitivity

This table presents the coefficients estimated in the logit CEO turnover model. The *Cultural Similarity Dummy* is equals one if *Cultural Similarity* is above the sample mean, and zero otherwise. *Involuntary CEO turnover* is a dummy variable that equals one if the CEO is forced out, and zero otherwise. All other variables are defined in **Table 5.3**. Standard errors are clustered at the firm level and t-statistics are reported in parentheses. ***, **, * denote statistical significance at the 1%, 5%, and 10% level, respectively.

	Involuntary CEO Turnover			
	(1)	**(2)**	**(3)**	**(4)**
Cultural Similarity Dummy	-3.481**	-0.238	-0.225	-3.036*
	(-2.263)	(-1.314)	(-1.240)	(-1.806)
Stock Return	-0.194			
	(-1.154)			
*Cultural Similarity Dummy*Stock Return*	0.695**			
	(2.083)			
Return on Assets		-0.004		
		(-0.620)		
Cultural Similarity Dummy Return on Assets*		0.017**		
		(2.221)		
Return on Sales			-0.000	
			(-0.750)	
*Cultural Similarity Dummy*ROS*			0.001*	
			(1.783)	
Sales Growth				-71.838**
				(-2.120)
*Cultural Similarity Dummy*Sales Growth*				65.880*
				(1.805)
Board Size	1.234***	1.021**	1.011**	1.077***
	(2.751)	(2.460)	(2.452)	(2.597)
Board Independence	1.898**	1.415*	1.287*	1.439*
	(2.380)	(1.886)	(1.697)	(1.907)
CEO Tenure	-0.066***	-0.066***	-0.061***	-0.063***
	(-3.452)	(-3.325)	(-3.103)	(-3.255)
CEO is Chair	-0.449	-0.425	-0.559	-0.531
	(-1.195)	(-1.238)	(-1.512)	(-1.472)
CEO Age	-0.027***	-0.022**	-0.023**	-0.025***
	(-2.791)	(-2.351)	(-2.446)	(-2.601)
Return Volatility	0.009**	0.008*	0.016*	0.008**
	(1.995)	(1.878)	(1.930)	(1.978)
Firm Size	-0.008	-0.041	-0.026	-0.029
	(-0.107)	(-0.611)	(-0.380)	(-0.433)
Intercept	-4.075***	-4.305***	-4.366***	3.263**
	(-2.791)	(-3.373)	(-3.348)	(2.092)
Industry FE	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes
Observations	3,211	3,358	3,352	3,355
Pseudo R2	0.0855	0.074	0.071	0.0761
Model significance	.	.	.	.
Likelihood ratio chi-square	65.75	90.85	86.66	92.29
p-value	0.0002	0.0007	0.0014	0.0004

5.4.5 CEO duality

Prior studies show that a CEO who is also the board chair has superior power and this dual leadership structure may challenge the board's ability to effectively monitor and discipline the CEO (Mallette and Fowler 1992; Goyal and Park 2002; Adams et al. 2005). Thus, given their lower likelihood of being replaced, a CEO who is also the chair of the board may have less to gain from having cultural ties with directors. To shed light on this issue, we examine whether CEO duality affects the association between CEO-board cultural similarity and involuntary turnover. We argue that CEOs who have cultural ties with the directors are less likely to be forced out if the CEO is also the board chair.

Table 5.12 exhibits the results on the impact of CEO duality on the relation between CEO-board cultural similarity and involuntary CEO turnover. We begin the analyses by regressing *Involuntary CEO Turnover* on the interaction term between *Cultural Similarity* and *CEO is Chair*. In column (1), the coefficient on the interaction term between *Cultural Similarity* and *CEO is Chair*, as the only explanatory variable, is negative (b=-1.041), and significant at the 5% level. Column (2) shows similar results after controlling for firm characteristics. Column (3) shows that the inclusion of both board and firm characteristics in the regression does not alter the sign or the significance of the *Cultural Similarity* (b=-2.140, p <.01). Column (4) shows similar results after controlling for the firm, board, and CEO characteristics. Consistent with our hypothesis, the coefficient on the *Cultural Similarity* is negative and statistically significant (b=-1.935, p <.10), indicating that CEO-board cultural similarity reduces the turnover rate when the CEO is the chair. Overall, **Table 5.12** exhibits that cultural similarity does not affect the likelihood of involuntary turnover when the CEO is not the chair, but exerts a negative influence on the involuntary turnover when the CEO is also the board chair

Concerning the control variables, we find that the estimated coefficients on the control variables in **Table 5.12** are generally as expected. The coefficient on *CEO Tenure* is significantly negative, implying that the CEO turnover is less likely when CEOs have longer tenure. The coefficient on *CEO Age* is negative and significant, indicating that older CEOs are less likely to be dismissed. We also find that the coefficients on *Board Size* and *Board Independence* are significantly positive in both logit regressions.

Finally, the coefficient on *Return Volatility* is negative and significant at the 10% level, which is consistent with Goyal and Park (2002).

Table 5. 12: CEO duality

This table presents the results of estimating equation (**5.1**) after including separate CEO-board cultural similarity variable for firms where the CEO is (is not) the board chair, i.e., the *Cultural Similarity* (0,1) – CEO is Chair (CEO is not chair) equals one if the firm has *Cultural Similarity* that is above the sample mean and is (not) the board chair, and zero, otherwise. *Involuntary CEO Turnover* is a dummy variable that equals one if the CEO is forced out, and zero otherwise. *Cultural Similarity* is the proportion of board directors that share similar ethnicity with the CEO. All other variables are defined in **Table 5.3**. Standard errors are clustered at the firm level and t-statistics are reported in parentheses. ***, **, * denote statistical significance at the 1%, 5%, and 10% level, respectively.

	Involuntary CEO turnover			
	(1)	**(2)**	**(3)**	**(4)**
Cultural Similarity (0,1)-CEO is not Chair	-0.204	-0.364	-0.363	-0.300
	(-1.237)	(-1.544)	(-1.456)	(-1.547)
Cultural Similarity (0,1)-CEO is Chair	-1.041**	-2.339**	-2.140**	-1.935*
	(-2.475)	(-2.244)	(-2.052)	(-1.890)
Board Size			1.104**	1.166***
			(2.379)	(2.623)
Board Independence			2.021**	1.782**
			(2.445)	(2.191)
CEO Tenure				-0.067***
				(-3.404)
CEO Age				-0.023**
				(-2.302)
Return on Assets		0.001	0.001	-0.000
		(0.258)	(0.158)	(-0.162)
Stock Return		-0.023	0.051	0.071
		(-0.140)	(0.315)	(0.439)
Return on Sales		0.000	-0.000	0.000
		(0.172)	(-0.028)	(0.165)
Sales Growth		7.046**	-26.464	-27.813
		(1.990)	(-1.251)	(-1.346)
Return Volatility		0.007	0.007	0.009*
		(1.512)	(1.571)	(1.867)
Firm Size		-0.008	-0.047	-0.021
		(-0.104)	(-0.620)	(-0.285)
Constant	-2.835***	-35.518**	115.477	122.907
	(-5.888)	(-2.185)	(1.184)	(1.291)
Year FE	Yes	Yes	Yes	Yes
Industry FE	Yes	Yes	Yes	Yes
N	4,506	3,063	3,015	3,011
Pseudo R2	0.012	0.052	0.065	0.083
Model significance				
Likelihood ratio chi-square	45.14	57.42	65.25	89.88
p-value	0.012	0.2194	0.086	0.001

5.4.6 Independent vs executive directors

Finally, we examine whether the consequences of CEO-board cultural similarity depend on whether such similarity is measured between the CEO and the independent directors or between the CEO and the non-independent directors (i.e., executive directors). According to prior literature (Fama 1980; Fama and Jensen 1983, Weisbach 1988), independent directors serve as effective monitors of senior managers, while the role of executive directors is mainly advisory. However, the question remains as to whether cultural similarity diminishes the monitoring effectiveness of independent directors.

If we discover that independent directors who share a similar cultural background with the CEO are also weak monitors, then the conventional measures of board independence would not encapsulate the inclination of the board to provide effective oversight and monitoring. Since independent directors have a stronger focus on monitoring, CEOs who share a similar cultural background with independent directors are less likely to be replaced. More specifically, we argue that cultural similarity should have a stronger influence on the involuntary turnover when a CEO shares a common culture with independent directors than when s/he is culturally linked to executive directors.

In this analysis, we construct two new variables. The first variable is the *Cultural Similarity-Independent* dummy, which equals one if the board consists of a majority of directors that are formally independent but culturally related to the firm's CEO, and zero otherwise. The other variable is the *Cultural Similarity-Dependent* dummy, which takes a value of one if the board consists of a majority of dependent/executive directors that are both formally and culturally related to the CEO, and zero otherwise.

The results are reported in **Table 5.13**. Column (1) shows that the coefficient on *Cultural Similarity-Independent* is negative (b=-0.402) and significant at the 10% level, whereas column (2) shows that the coefficient on *Cultural Similarity-Executive* is negative, but insignificant, implying that the effect of cultural similarity on CEO involuntary is driven by the CEO's connections with independent rather than executive directors.

This evidence suggests that the CEO-board cultural ties weaken the effectiveness of board monitoring and subsequently reduce the probability of forced turnover. The

negative effect of cultural similarity on involuntary CEO turnover is more concentrated among boards with formally independent directors, as cultural ties may prevent conventionally independent directors from performing their monitoring functions. Another implication of these results is that, once a director is culturally tied with the CEO, her/his independence becomes less important from a monitoring perspective. This could also explain why prior research documents equivocal evidence on the relation between board independence and various measures of governance outcomes, particularly CEO turnover (Laux 2008; Kaplan and Minton 2012; Dah et al. 2014).

The results of the control variables are generally consistent with prior literature. Specifically, in line with the previous research (Goyal and Park 2002; Hermalin and Weisbach 2003; Dikolli et al. 2014), we find that the coefficient on *CEO Tenure* is negative and significant at the 1% level, implying that longer-tenured CEOs are less likely to be forced out. Consistent with Core et al. (1999) and Balsam et al. (2017), we also find that the coefficient on *CEO Age* is negative and significant at the 5% level, indicating that older directors tend to be negatively associated with forced turnover. We also find that the coefficients on *Board Size* and *Board Independence* are positive and significant across the logit regressions, indicating that firms with larger board and higher proportion of independent directors are associated with increased involuntary turnover. Finally, the results also show that the coefficient on *Return Volatility* is positive and significant at the 10% level, implying that firms with higher stock return volatility are positively associated with forced turnover, which is in line with Balsam et al. (2017) and Hazarika et al. (2012).

Table 5. 13: Independent vs. executive directors

This table reports the coefficients estimated in the logit CEO turnover models. *Involuntary CEO Turnover* is a dummy variable that equals one if the CEO is forced out, and zero otherwise. *Cultural Similarity-Independent* and *Cultural Similarity-Executive* are the measures of CEO-board cultural similarity computed for independent and executive directors, respectively. All other variables are defined in **Table 5.3**. Standard errors are clustered at the firm level and t-statistics are reported in parentheses. ***, **, * denote statistical significance at the 1%, 5%, and 10% level, respectively.

	Involuntary CEO Turnover	
	(1)	**(2)**
Cultural Similarity-Independent	-0.402*	
	(-1.819)	
Cultural Similarity-Executive		-0.553
		(-1.035)
Board Size	1.156**	1.166***
	(2.574)	(2.621)
Board Independence	2.204***	1.544*
	(2.579)	(1.829)
CEO Tenure	-0.067***	-0.067***
	(-3.454)	(-3.405)
CEO is Chair	-0.599	-0.609
	(-1.464)	(-1.510)
CEO Age	-0.023**	-0.022**
	(-2.371)	(-2.279)
Return on Assets	0.000	-0.001
	(0.002)	(-0.245)
Stock Return	0.071	0.070
	(0.431)	(0.431)
Return on Sales	0.000	0.000
	(0.326)	(0.232)
Sales Growth	-27.078	-28.342
	(-1.302)	(-1.364)
Return Volatility	0.009*	0.009*
	(1.904)	(1.865)
Firm Size	-0.013	-0.007
	(-0.173)	(-0.095)
Constant	119.396	125.279
	(1.245)	(1.308)
Industry FE	Yes	Yes
Year FE	Yes	Yes
Observations	3,014	3,014
Pseudo R2	0.079	0.080
Model significance		
Likelihood ratio chi-square	85.16	87.08
p-Value	0.002	0.001

5.4.7 Cultural diversity and involuntary CEO turnover

Despite the effort of this thesis in investigating the effect of cultural similarity between CEO and board members, we also include an analysis on the effect of cultural diversity on CEO turnover to complement our study. A long-established tradition of research on corporate governance emphasises that CEOs prefer less vigilance and control by the board (Westphal and Zajac 2013). Nevertheless, a more diverse board is likely to evaluate CEO's strategic decisions and actions from a range of perspectives, potentially monitoring managerial decisions and actions more vigorously and can potentially result in better monitoring effectiveness (Adams and Ferreira 2009; Adams et al. 2015). Due the diverse backgrounds offer directors to draw from a wider range of perspectives in advising and monitoring the CEOs, many boards have responded to the pressure from shareholders by increasing their degree of cultural/ethnic diversity. Given that cultural diversity is a primary influence of the CEO-board relationship, we expect that cultural diversity may improve board independence and effectiveness and those firms with high cultural diversity between CEOs and board of directors are more likely to remove underperforming CEOs, leading to an increased involuntary CEO turnover.

Therefore, in this section, we evaluate the impact of CEO-board cultural diversity on involuntary CEO turnover. We introduce a new measure of cultural diversity (*Cultural Diversity),* defined as the proportion of board of directors that has diverse ethnic or cultural background with the CEO.

Table 5.14 exhibits the impact of CEO-board cultural diversity on involuntary CEO turnover. We begin the analyses by regressing *Forced/Involuntary CEO Turnover* on *Cultural Diversity*. In column (1), the coefficient on *Cultural Diversity*, as the only explanatory variable, is positive ($b=0.612$), and significant at the 1% level. Column (2) shows similar results after firm characteristics are introduced ($b=0.834$, $p<.01$). Column (3) presents the test results after controlling for both board and firm characteristics. The inclusion of the two groups of control variables also does not alter the sign or the significance of the *Cultural Diversity* ($b=0.824$, $p<.01$). Column (4) shows similar results after controlling for the firm, board, and CEO characteristics. Consistent with our hypothesis, the coefficient on the *Cultural Diversity* is positive

and statistically significant ($b=0.744$, p <.01), indicating that CEO-board diversity increases the involuntary CEO turnover rate, which supports our argument in this section**.**

The results of the control variables are generally consistent with prior literature. Specifically, in line with the previous research (Goyal and Park 2002; Hermalin and Weisbach 2003; Dikolli et al. 2014), we find that the coefficient on *CEO Tenure* is negative and significant at the 1% level, implying that longer-tenured CEOs are less likely to be forced out. Consistent with Core et al. (1999) and Balsam et al. (2017), we also find that the coefficient on *CEO Age* is negative and significant at the 5% level, indicating that older directors to be negatively associated with forced turnover. We also find that the coefficients on both *Board Size* and *Board Independence* are positive and significant, indicating that firms with larger board and higher proportion of independent directors are associated with increased involuntary turnover. Finally, the results also show that the coefficient on *Return Volatility* is positive and significant at 10% level, implying that firms with higher stock return volatility are positively associated with forced turnover, which is in line with Balsam et al. (2017) and Hazarika et al. (2012).

Overall, in this section, we show that cultural diversity within CEO-board dyad provide opposite outcomes as compared to CEO-board cultural similarity in our main analyses. The results also consistent with the studies on the positive impacts of board diversity on organisation incomes (Erhardt et al. 2003; Adams and Ferreira 2009; Adams et al. 2015). These studies show that the board diversity is associated with better governance and those diverse boards are more likely to remove underperforming CEOs, leading to an increased involuntary CEO turnover.

Table 5. 14: Cultural diversity and involuntary CEO turnover

This table reports the coefficients estimated in the logit CEO turnover models. *Involuntary CEO Turnover* is a dummy variable that equals one if the CEO is forced out, and zero otherwise. *Cultural Diversity* is the proportion of board directors that has diverse ethnicity with the CEO. All other variables are defined in **Table 5.3**. Standard errors are clustered at the firm level and t-statistics are reported in parentheses. ***, **, * denote statistical significance at the 1%, 5%, and 10% level, respectively.

	Involuntary CEO Turnover			
	(1)	**(2)**	**(3)**	**(4)**
Cultural Diversity	0.612***	0.834***	0.824***	0.744***
	(3.165)	(3.941)	(3.749)	(3.539)
Board Size			1.202***	1.179***
			(2.659)	(2.692)
Board Independence			2.074**	1.786**
			(2.459)	(2.182)
CEO Tenure				-0.063***
				(-3.342)
CEO is Chair				-0.556
				(-1.392)
CEO Age				-0.025**
				(-2.530)
Return on Assets		0.000	0.000	-0.000
		(0.103)	(0.040)	(-0.105)
Stock Return		-0.041	0.033	0.058
		(-0.240)	(0.197)	(0.352)
Sales Growth		7.332**	-25.941	-26.351
		(2.129)	(-1.209)	(-1.299)
Return on Sales		-0.000	-0.000	-0.000
		(-0.090)	(-0.267)	(-0.053)
Return Volatility		0.007	0.007*	0.009*
		(1.567)	(1.646)	(1.940)
Firm Size		-0.007	-0.054	-0.027
		(-0.098)	(-0.675)	(-0.348)
Intercept	-3.074***	-36.993**	112.739	116.198
	(-6.197)	(-2.339)	(1.139)	(1.243)
Year FE	Yes	Yes	Yes	Yes
Industry FE	Yes	Yes	Yes	Yes
Observations	4,510	3,063	3,015	3,011
Pseudo R2	0.045	0.052	0.062	0.088
Model significance				
Likelihood ratio chi-square	94.21	98.61	100.67	476.09
p-value	0.000	0.000	0.000	0.000

5.5 Conclusion

To present another potential cause of the negative valuation impact of CEO-board cultural similarity, we have explored the relationship between CEO-board cultural similarity and managerial entrenchment as reflected in involuntary CEO turnover.

The most important findings are highlighted:

First, we find that CEO-board cultural similarity reduces the risk of involuntary CEO turnover. Our results hold after implementing the two-stage least squares (2SLS) instrumental variable approach as an endogeneity test and are robust to alternative measurements and model specifications.

Second, we also find that CEO-board cultural similarity is associated with lower turnover performance sensitivity, implying that, given that the cultural ties with directors may facilitate bond, empathy, and trust between them, these CEOs are thus less likely to be replaced, even when they achieve poor performance

Third, our results also indicate that CEO-board cultural similarity reduces the turnover rate when the CEO is the chair. Nevertheless, we find no evidence that cultural similarity affects the likelihood of involuntary turnover when the CEO is not a chair.

Fourth, we also find that the negative consequences of cultural similarity are prevalent when CEOs share a similar culture with independent rather than executive directors. This indicates that cultural ties may prevent conventionally independent directors from performing their monitoring functions, suggesting that the CEO-board cultural ties weaken the effectiveness of board monitoring and subsequently reduce the risk of involuntary turnover. Finally, we find that cultural diversity increases the risk of involuntary CEO turnover.

Overall, the findings from this chapter suggest that CEO-board cultural similarity could also lead to higher managerial entrenchment, which could be reflected through the reduced likelihood of dismissing poorly performing CEOs. This could be one of the potential causes of the negative valuation impact of CEO-board cultural similarity evidenced in **Chapter 3**.

Chapter 6

Conclusion

6.1 Introduction

The thesis contributes to our understanding of the impact of CEO-board cultural similarity on firm valuation and the effectiveness of the board of directors. While prior studies have long emphasised the effect of social ties on governance outcomes, we know little about the cultural ties. This thesis indicates that cultural similarity can be an indicator of the existence of similar values and beliefs between CEO and directors, which can potentially be either detrimental or beneficial. Accordingly, this thesis investigates whether this new type of manager-director ties, resulting from cultural similarity, affects firm valuation based on the competing hypotheses. Further, this thesis investigates the potential causes of the negative valuation impact of CEO-board cultural ties. It explores whether the cultural similarity between the CEO and board of directors affects the quality of financial reporting, as proxied by earnings management. Furthermore, the thesis examines whether the cultural similarity between the CEO and other board members is associated with managerial entrenchment, as measured by involuntary CEO turnover. The findings of these investigations extend and complement the existing corporate governance research relating to: i) the ramifications of CEO-board social ties, ii) the determinants of weak internal control and inefficient board monitoring, iii) the role of culture in finance and corporate governance, iii) earnings management, and iv) CEO turnover. Similarly, this thesis also has major implications for various stakeholders such as investors, policymakers, and regulators.

The main objective of this thesis was to investigate whether the CEO-board cultural similarity affects firm valuation and the effectiveness of the board of directors. To achieve this objective, the thesis focused on the following questions. ***First,*** does CEO-board cultural similarity influence firm value? ***Second***, what are the potential causes of the negative valuation impact of CEO-board cultural similarity? ***Third***, does CEO-board cultural similarity influence board independence and the effectiveness of the

board of directors' monitoring function? These objective and questions form the basis of the three empirical chapters in this thesis (i.e., **Chapter 3**, **Chapter 4**, and **Chapter 5**).

The remainder of this chapter is organised as follows:

Section 6.2 will present the key findings of the three empirical chapters. **Section 6.3** will discuss the theoretical contributions of this thesis. **Section 6.4** will highlight the policy and practical implications based on the thesis findings. **Section 6.5** will discuss the thesis limitations and, finally, **Section 6.6** will highlight some areas and several suggestions for future research.

6.2 Key findings of the empirical chapters

CEO-board cultural similarity and firm value

Chapter 3 examines the effects of the cultural similarity between CEO and board of directors on firm value. As suggested by prior literature[19], strong CEO-director ties can be either detrimental or beneficial. On the one hand, the strong ties between the CEO and board of directors facilitate quicker and more systematic decision-making, enhance information flow, and improve the board's advisory function, leading to increases in firm value. On the other hand, the CEO's ties with the board members can also result in greater managerial entrenchment and opportunism resulting from ineffective monitoring by the board, leading to decreases in firm value. In this chapter, we empirically examine the value implications of cultural similarity between the CEO and board of directors. We do so by utilising a rich dataset of Malaysian listed firms over the period 2009 to 2016. The analyses from this chapter document several interesting results.

First, using OLS regressions, the results from the baseline analysis show a lower Tobin's Q for firms with a higher percentage of cultural similarity between the CEO and other board members. The results remain consistent after controlling for the board

[19] Among these studies are Hwang and Kim (2009), Fracassi and Tate (2012), Krishnan et al. (2011), Hoitash (2011), Lee et al. (2014) and Fan et al. (2019)

and firm characteristics. In terms of economic significance, a one-standard-deviation increase in cultural similarity is associated with a 6.14% decline in firm value. In conducting robustness tests, several alternative model specifications and variable definitions were employed. In addressing the endogeneity test, several approaches were also employed, including firm fixed effect, propensity score model, and instrumental variables approach. Indeed, the results show that CEO-board cultural similarity reduces firm value even after conducting several robustness tests and endogeneity tests.

Second, this chapter further examines whether greater CEO-board cultural similarity results in fewer board meetings. Using the fixed effect model, the results show a lower number of board meetings for firms with a higher percentage of cultural similarity between the CEO and other board members. The results suggest that cultural similarity between the CEO and other board members reduces the frequency of board meetings and, therefore, decreases board vigilance and monitoring.

Third, motivated by existing studies that incorporate the social ties into the definition of true independence (e.g., Hwang and Kim 2009), this chapter further examines the differential association between board independence and firm value when the formal measure of board independence (which does not consider CEO-board cultural ties) is replaced with the new measure of board independence. Under the new measure, a director is identified as independent if he or she is an independent director and also culturally independent from the CEO. The results indicate a positive relationship between the new proposed measure and firm value. These results suggest that cultural ties are value-relevant and matter and act as a medium of CEO-board relationship, which consequently may impair the effectiveness of board independence.

Fourth, as an additional test of the relevance of cultural similarity ties to board monitoring, this chapter investigates whether the negative relation between cultural similarity and firm value differs among dependent (executive) or independent directors. The analyses reveal that the negative effect of cultural similarity on firm value is more concentrated among the independent directors. Thus, this study suggests that cultural ties may prevent conventionally independent directors from performing their monitoring functions.

Finally, this chapter further investigates whether the political connections influence the negative association between cultural similarity and firm value. The results show that the negative effect of cultural similarity on firm value is similar even after controlling for political connections as proxied by Malay CEO and board, implying that the results are not driven by political connections.

Overall, the results of the analyses from this chapter indicate that cultural similarity can potentially weaken the board independence and monitoring effectiveness of board members, and ultimately destroy firm value.

CEO-board cultural similarity and earnings management

Chapter 4 explores one of the potential causes of the negative valuation impact of CEO-board cultural similarity. Specifically, this chapter examines whether the cultural similarity between the CEO and board of directors affects the quality of financial reporting. This chapter argues that the presence of cultural similarity between the board and CEOs may jeopardise the board's monitoring role in ensuring fair and unbiased reporting. As a result of the board's reduced monitoring, CEOs are more likely to act and make decisions in their own interests; for example, engage in earnings management practice to smooth earnings. In this chapter, we empirically examine the effects of cultural similarity between the CEO and board members on earnings management. By doing so, this chapter employs Malaysian data of 3,588 firm years from 2009 to 2016 in the Bursa Malaysia. The analyses from this chapter exhibit several important results.

First, by employing OLS regression, the baseline results report a positive and significant relation between CEO-board cultural similarity and income-increasing accrual-based earnings management, implying that firms with a higher cultural similarity between CEO and board of directors are more likely to engage in income-increasing accrual-based earnings management. The results are robust to an endogeneity check, which employs the instrumental variable approach. Two instrumental variables are used in 2SLS regression, namely the first lag of the CEO-board cultural similarity measure and the industry mean cultural similarity measure. The results remain consistent by using an alternative measure of earnings management (i.e., real-earnings management).

Second, this chapter further investigates whether the positive effect remains consistent after controlling for CEO power. In this study, we use CEO duality as a proxy for CEO power. The analysis finds that firms with a higher cultural similarity between CEOs and the board of directors are more likely to engage in income-increasing accrual-based earnings management as well as income-increasing real-earnings management, even after controlling for CEO power.

Third, several existing studies argue that the formally defined board independence does not account for the presence of social ties and pre-existing network connections between CEO and independent directors, which are associated with weaker internal governance (Hwang and Kim 2009; Krishnan et al. 2011). Thus, we propose a culturally-adjusted measure of board independence to investigate the extent to which the cultural independence between CEO and independent directors is relevant to earnings management practice. The results show that the negative effect of board independence on income-increasing (accrual-based) earnings management is evident in a truly independent board, i.e., board members do not have any formal or cultural ties with the CEO. The results imply that boards are more effective at controlling agency issues and limiting managerial opportunism when they are both formally and culturally independent.

Fourth, this chapter further explores whether the positive effect of cultural similarity on earnings management differs among the dependent (executive) and independent directors. The positive effect of CEO-board cultural similarity on income-increasing accrual-based earnings management is more concentrated among the independent directors. Thus, the findings suggest that cultural similarity prevents independent directors from performing their monitoring role effectively.

Finally, this chapter considers the implication of CEO-audit committee cultural similarity on earnings management. Specifically, this study repeats the main analysis after redefining the variable of interest as the fraction of audit-committee members who share a similar culture to the CEO. Using a similar OLS regression, this study, however, finds no evidence on the relations between the CEO-audit committee cultural similarity and earnings management.

Overall, the findings from this chapter highlight that CEO-board cultural similarity could also lead to weak internal control over financial reporting quality, which is

proxied by CEO's engagement in earnings management. This could be one of the potential sources of the negative valuation impact of cultural similarity that was evident in **Chapter 3**.

CEO-board cultural similarity and involuntary turnover

Chapter 5 further explores another potential reason for the negative valuation impact of CEO-board cultural similarity. This chapter examines whether the cultural similarity between the CEO and other board members is associated with managerial entrenchment. Specifically, the chapter empirically investigates the association between CEO-board cultural similarity and involuntary turnover. As suggested by prior studies (Hwang and Kim 2009; Nguyen 2012; Kramarz and Thesmar 2013; Balsam et al. 2017), socially dependent boards have lower CEO turnover risk than firms whose boards are socially independent, and these studies also assert that the CEO-director ties are associated with reduced involuntary CEO turnover. Following prior research, this study defines turnover as involuntary if there is a CEO change between year t and t + 1 and the departing CEO is less than 60 years old (Coles et al. 2014; Balsam et al. 2017). The analyses from **Chapter 5** exhibit several important results.

By employing a large panel dataset and logit regression analysis of the Malaysian listed firms between 2009 and 2016, **Chapter 5** has shown that CEO-board cultural similarity influences involuntary turnover. The baseline analysis shows a negative and significant association between CEO-board cultural similarity and involuntary turnover, indicating that the presence of CEO-board cultural similarity reduces the probability of involuntary turnover. The results remain consistent when employing various alternative measurements and specifications as well as being robust to an endogeneity test, which is conducted by using the instrumental variables approach.

The second analysis further explores the impact of CEO-board cultural similarity on the relationship between CEO turnover and firm performance. Given that their cultural ties with directors may facilitate bond, empathy, and trust between them, these CEOs are thus less likely to be replaced, even when they achieve poor performance. Specifically, this chapter argues that CEO-board cultural similarity is associated with lower turnover performance sensitivity. Consistent with the argument, the logit

regression analysis shows evidence that CEO-board cultural similarity is associated with lower turnover performance sensitivity

The third analysis further explores whether CEO duality affects the associations between cultural similarity and involuntary turnover. This study argues that a CEO who has cultural ties with the directors is less likely to be fired if s/he is also a board chair. Consistent with the prediction, the results indicate that CEO-board cultural similarity reduces the turnover rate when the CEO is the chair. However, the study finds no evidence that cultural similarity affects the likelihood of involuntary turnover when the CEO is not the chair.

Having illustrated the negative impact of CEO-board cultural similarity on forced CEO turnover, this chapter further analyses whether the effect of cultural similarity is equal when similarity is measured among the independent or executive directors. The fourth analysis has shown that it is the cultural similarity between CEO and independent directors, rather than that between CEO and executive directors, that is negatively related to involuntary CEO turnover. This indicates that cultural ties may prevent conventionally independent directors from performing their monitoring functions, suggesting that the CEO-board cultural ties weaken the effectiveness of board monitoring and subsequently reduce the risk of involuntary turnover.

Overall, the findings from this chapter suggest that CEO-board cultural similarity could also lead to lower board monitoring effectiveness and higher managerial entrenchment, which could be reflected through the reduced likelihood of dismissing poorly performing CEOs.

6.3 Empirical contributions

The theory and several supportive findings from this thesis make several significant contributions to the nascent literature on corporate governance.

First, this thesis complements and extends corporate governance literature by introducing the new type of manager-director ties, arising from cultural similarity, and investigating how such ties affect firm valuation and the monitoring effectiveness of the board. Prior research on corporate governance that has incorporated the behavioural perspective accentuated the influence of socio-psychological factors, such

as social ties among key governance actors (Westphal and Zajac 2013). Correspondingly, myriad studies explore how the social reciprocity between CEO and directors influence the board effectiveness and governance outcomes (e.g., Hwang and Kim 2009; Krishnan et al. 2011; Nguyen 2012) as well as firm valuation (e.g., Fracassi and Tate 2012; Lee et al. 2014; Goergen et al. 2015). These studies emphasise the relationship that is constructed via board interlocks, professional, education, and employment background, which has been characterised as achieved ties (e.g., Hwang and Kim 2009; Krishnan et al. 2011; Fracassi and Tate 2012). However, to the best of our knowledge, there exists no previous empirical work concerning how cultural ties between CEO and directors affect corporate governance outcomes. Hence, this thesis yields fresh insight on the consequence of CEO-board cultural similarity on firm value and the monitoring effectiveness of the board. In particular, the findings from this thesis imply that CEO-board cultural similarity also matters, and such similarity impairs the firm value and the monitoring effectiveness of the board. Furthermore, this thesis also identifies potential channels through which CEO-board cultural similarity can decrease firm value.

Second, this thesis adds to the numerous literature on the determinants of weak internal control and inefficient board monitoring by taking cultural ties into account. Prior studies investigate the role of the formal system, such as board structure and composition, that limit the managers performing unethical activities and diminish agency costs. Nevertheless, a burgeoning strand of literature has recently recognised the influence of the informal system, such as corporate culture, cultural norms, and social factors (e.g., Guiso et al. 2006, 2009, 2015). Thus, motivated by this line of literature, this thesis investigates whether and how cultural ties as an informal system influence internal control and board monitoring by examining how CEO-board cultural ties influence managerial entrenchment and financial reporting quality.

Third, this study sheds light on the influence of culture/ethnicity in finance and corporate governance. Due to the importance of culture as an informal system as well as social identity, a flourishing body of governance studies have attempted to explain the role of culture in business practice, corporate decision-making, and organisational outcomes (e.g., Zheng et al. 2012; Ahern et al. 2015; El Ghoul and Zheng 2016). Prior literature also suggests that cultural similarity has been evidenced to facilitate mutual trust and lubricate economic exchange (Guiso et al. 2009; Shi and Tang 2015).

However, the evidence on the role of culture within corporate boards is still scarce. Therefore, this thesis fills the void by examining the effect of cultural similarity between CEO and board on firm value and board monitoring. Specifically, this thesis also complements and extends the limited studies on the role of culture within the corporate governance area (e.g., Li and Harrison 2008; Bryan et al. 2015; Frijns et al. 2016; Nguyen et al. 2018) by suggesting that cultural ties between CEO and directors reduce the effectiveness of board monitoring and internal control, leading to decreases in firm value. Moreover, the thesis also reveals how cultural ties affect financial reporting quality through earnings management practice and managerial entrenchment, which could be reflected through the reduced likelihood of dismissing poorly performing CEOs.

Fourth, this thesis contributes to the extant literature on executives' incentives to manage earnings. Prior research has attempted to explain the firm's motives and managerial incentives for earnings management and the reasons for such opportunistic and self-serving behaviour (Burgstahler and Dichev 1997; DeGeorge et al. 1999; Bergstresser and Phillipppon 2006; Burns and Kedia 2006). Evidence suggests that managers are generally prone to manipulate earnings in response to their bonus schemes, stock, and options holdings (Healy 1985; Bergstresser and Phillipppon 2006; Burns and Kedia 2006). Prior studies suggest that the social ties between CEO and board as well as between CEO and audit committee influence financial reporting quality and earnings management (Hwang and Kim 2012; Krishnan et al. 2011; Bruynseels and Cardinaels 2014). However, little is known about the effect of cultural ties between managers and the board on earnings management. Thus, our study complements and extends the literature by offering evidence that CEO-board cultural ties may also spur managers to manipulate earnings as well as engage in distinctly different forms of earnings management.

Finally, this thesis also contributes to corporate governance research on CEO turnover by identifying a new mechanism through which CEOs can influence involuntary turnover. It provides new insights into the literature by showing that CEO characteristics, such as the CEO's cultural connections with other board members, represent an important source of managerial entrenchment. In particular, the findings from this thesis show that CEO-board cultural similarity protects poor-performing managers from dismissal.

6.4 Practical and policy implications

The findings from this thesis have several crucial implications for various stakeholders including shareholders, policymakers, and regulators.

First, the results from this thesis suggest that shareholders should consider and focus on the relevance of CEO-board cultural ties. Generally, investors designate a board of directors to monitor executives on their behalf due to the imperfect information regarding managerial behaviour, activities, and contribution. Nevertheless, the monitoring role of the board may be jeopardised, particularly when directors share a similar cultural background to executives. The findings from this thesis suggest that CEO-board cultural similarity weakens internal control and board monitoring and results in decreased firm value.

Second, the results from this thesis are relevant to the firm's corporate governance and internal control. The thesis indicates that the CEO-board cultural ties reduce board monitoring effectiveness and financial reporting quality. Hence, to enhance the quality of financial information and decrease the managerial entrenchment and opportunism, firms need to improve their internal quality by considering cultural ties in their decisions, particularly in the appointment of the CEO and board of directors.

Furthermore, the findings from this thesis are also informative to policymakers and regulators, such as the Securities Commission Malaysia, who aim to improve the regulations for better corporate governance and the effectiveness of the board of directors. The current regulations define director independence exclusively in terms of financial or familial ties to the CEO or the firm. Nevertheless, this thesis suggests that, although these requirements may be relevant, true independence can only be achieved by limiting the CEO-board cultural ties.

6.5 Research limitations

While this research has reached its main objectives and provides significant insights into the way CEO-board cultural similarity affects firm value and board monitoring in Malaysia, there were several unavoidable bottlenecks in the research. Hence, these possible limitations should be acknowledged when interpreting the research findings. This research has three caveats and limitations, which are explained below.

First, since the findings are based on the empirical context of Malaysian listed firms, we must reflect on the generalisability of the results. In particular, the research findings are grounded on the unique features of a multicultural setting, where interpersonal ties and social networks are crucial in the business environment and people attach importance to clan culture and ethnic groups. Hence, the results should be reasonably supported and generalisable in other Asian contexts (e.g., Singapore) that share similar environments and institutional settings. However, the generalisability of the results to countries that have different institutional settings, cultures, and corporate governance systems may be restricted. Therefore, readers should be cautious about generalising the findings of this study to all markets before conducting further analysis.

Second, as common to numerous governance studies, this research is also subject to potential endogeneity. For example, a firm's decision to appoint a CEO with a similar cultural background to other directors is not randomised, and, hence, our results may be subject to potential self-selection bias. Moreover, there is a reverse causality concern, especially between CEO-board cultural similarity and firm performance, as high-performing firms may also adopt strategies that lower CEO-board cultural similarity and improve cultural diversity, or vice versa. Another potential endogeneity concern in this research is omitted variables. Since control variables are varied across corporate governance research (i.e., CEO turnover), thus, the potential for omitted variables is highly present. Nevertheless, such endogeneity concerns are addressed in this study with the use of instrumental variables, propensity score matching, firm fixed effects, lagged independent variables, and multiple control variables. Despite the efforts in addressing the endogeneity concerns through these approaches, however, we cannot entirely rule out the effect of endogeneity.

Third, as culture has always been demonstrated as “a fuzzy, difficult-to-define and construct” (Triandis et al. 1986, p.258), it is indeed difficult to quantify and measure. Therefore, the measurement of culture in this empirical study was restricted to one of the basic dimensions of culture, which is ethnicity. Nevertheless, ethnicity has been closely related to culture and is greatly relevant in the Malaysian cultural context; thus, the measurement of culture in this empirical study was focused on the ethnicity of CEO and directors. Nevertheless, it has to be kept in mind that the ethnicity attribute is not the only measure of determining the cultural background of directors; thus, the measurement of culture in this study also may not apply to different countries that

have different cultures and institutional environments. Nonetheless, the research findings as well as the limitations of this study have opened up avenues for future research opportunities. This will be discussed in the next section.

6.6 Suggestions for further research

The findings in this thesis offer several suggestions for future research and can be extended and developed further in different various ways, which are described below.

First, while this research has focused on the effects of cultural similarity between CEO and board of directors on firm value and board monitoring, future research could examine how this similarity influences other governance outcomes and major corporate decisions such as risk-taking, acquisitions, CEO succession, and CEO compensation. For instance, our theory would suggest that directors' cultural ties with CEOs may also influence CEO succession decisions and CEO compensation. Furthermore, other scopes of observation could be extended to other key governance constituents such as CFO or nomination committees as well as remuneration committees to analyse how cultural ties influence their roles.

Second, while our single country setting has some potentially interesting lessons for other emerging economies, it is implausible to entirely capture heterogeneity that may be present in investigating the influence of cultural ties among the developing countries. This is because every country is different in terms of its formal system, political system, cultural influence, economy, and financial market. Therefore, future studies may wish to examine whether and how CEO-board cultural ties, operationalised in the current study, affect firm value and board effectiveness in cross-country settings of various developing countries in the world with the same institutional environment and cultural influence. Furthermore, while the findings of the current study are more generalisable to undeveloped formal systems and relation-based business settings, future studies can also examine whether cultural ties matter in Western economies, such as in the US, which has one of the most complex cultural identities in the world.

Third, this study focuses on ethnicity, one of the basic cultural dimensions used to capture the cultural background of CEO and directors. Future studies could adopt more

refined measures of CEO and directors' cultural background to test the current study's theory by using different dimensions of culture, such as religion or language. Investigating the influence of other aspects of cultural variations may provide some fresh insights into understanding the role of cultural values in affecting the CEO-board relationships as well as firm behaviours. Furthermore, future studies could also use a longitudinal survey or other qualitative studies to gain more insights into the influence of CEO-board cultural ties on several organisational outcomes.

References

Abdullah, A. 1992. The influence of ethnic values on managerial practices in Malaysia. *Malaysian Management Review* 27, pp. 9-17.

Abdullah, A. 1996. *Going glocal: Cultural dimensions in Malaysian management*. Malaysia: Malaysian Institute of Management.

Abdullah, A. 2005. Cultural dimensions of Anglos, Australians and Malaysians. *Journal of International Business, Economics and Entrepreneurship (JIBE)* 2(2), pp. 21-33.

Abdullah, S.N. et al. 2016. Does having women on boards create value? The impact of societal perceptions and corporate governance in emerging markets. *Strategic Management Journal* 37(3), pp. 466-476.

Abdul Wahab, E.A.A. et al. 2015. Political connections: A threat to auditor independence? *Journal of Accounting in Emerging Economies* 5(2), pp. 222-246

Abraham, C.E. 1997. *Divide and rule: The roots of race relations in Malaysia*. Kuala Lumpur, Malaysia: INSAN.

Adams, R.B. 2003. What do boards do? Evidence from board committee and director compensation data. *SSRN*. http://dx.doi.org/10.2139/ssrn.397401

Adams, R.B. and Ferreira, D. 2007. A theory of friendly boards. *The Journal of Finance* 62(1), pp. 217-250.

Adams, R.B. et al. 2005. Powerful CEOs and their impact on corporate performance. *The Review of Financial Studies* 18(4), pp. 1403-1432.

Adler, P.S. and Kwon, S.W. 2002. Social capital: Prospects for a new concept. *Academy of Management Review* 27(1), pp. 17-40.

Aggarwal, R. et al. 2012. Gravity and culture in foreign portfolio investment. *Journal of Banking & Finance* 36(2), pp. 525-538.

Aggarwal, R. et al. 2016. Culture and finance: An introduction. *Journal of Corporate Finance* 100(41), pp. 466-474.

Agrawal, A. and Chadha, S. 2005. Corporate governance and accounting scandals. *The Journal of Law and Economics* 48(2), pp. 371-406.

Aguilera, R.V. et al. 2008. An organizational approach to comparative corporate governance: Costs, contingencies, and complementarities. *Organization Science* 19(3), pp. 475-792

Aguilera, R.V. and Jackson, G. 2010. Comparative and international corporate governance. *Academy of Management Annals* 4(1), pp. 485-556.

Ahern, K.R. et al. 2015. Lost in translation? The effect of cultural values on mergers around the world. *Journal of Financial Economics* 117(1), pp. 165-189

Ahmad-Zaluki, N.A. 2012. Board ethnic diversity in newly listed Malaysian companies. *Indian Journal of Corporate Governance* 5(1), pp. 24-32.

Alba, R.D. 1990. *Ethnic identity: The transformation of white America*. New Haven, CT: Yale University Press.

Alchian, A.A. and Demsetz, H. 1972. Production, information costs, and economic organization. *The American Economic Review* 62(5), pp. 777-795.

Allen, F. et al. 2005. Law, finance, and economic growth in China. *Journal of Financial Economics* 77(1), pp. 57-116.

Alnasser, S. 2012. What has changed? The development of corporate governance in Malaysia. *The Journal of Risk Financ*e 13(3), pp. 269-276

Anderson, R.C. et al. 2011. The economics of director heterogeneity. *Financial Management, 40*(1), pp.5-38.

Andres, C. 2008. Large shareholders and firm performance—An empirical examination of founding-family ownership. *Journal of Corporate Finance* 14(4), pp. 431-445.

Arrow, H. et al. 2000. *Small groups as complex systems: Formation, coordination, development, and adaptation*. Thousand Oaks, CA: Sage Publications.

Arthaud-Day, M.L. et al. 2006. A changing of the guard: Executive and director turnover following corporate financial restatements. *Academy of Management Journal* 49(6), pp. 1119-1136.

Ashforth, B.E. and Mael, F. 1989. Social identity theory and the organization. *Academy of Management Review* 14(1), pp. 20-39.

Balsam, S. et al. 2017. Network connections, CEO compensation and involuntary turnover: The impact of a friend of a friend. *Journal of Corporate Finance* 45, pp. 220-244.

Baskerville, R.F. 2003. Hofstede never studied culture. *Accounting, Organizations and Society* 28(1), pp. 1-14.

Baskerville-Morley, R.F. 2005. A research note: the unfinished business of culture. *Accounting, Organizations and Society* 30(4), pp. 389-391.

Beasley, M.S. 1996. An empirical analysis of the relation between the board of director composition and financial statement fraud. *Accounting Review* 71(4), pp. 443-465.

Becker, C.L. et al. 1998. The effect of audit quality on earnings management. *Contemporary Accounting Research* 15(1), pp. 1-24.

Bédard, J. et al. 2004. The effect of audit committee expertise, independence, and activity on aggressive earnings management. *Auditing: A Journal of Practice & Theory* 23(2), pp. 13-35.

Belderbos, R. et al. 2004. Cooperative R&D and firm performance. *Research Policy* 33(10), pp. 1477-1492.

Benhabib, S. 2002. *The claims of culture: Equality and diversity in the global era*. Princeton, NJ: Princeton University Press.

Bergstresser, D. and Philippon, T. 2006. CEO incentives and earnings management. *Journal of Financial Economics* 80(3), pp. 511-529.

Betancourt, H. and López, S.R. 1993. The study of culture, ethnicity, and race in American psychology. *American Psychologist* 48(6), pp. 629.

Beugelsdijk, S. and Frijns, B. 2010. A cultural explanation of the foreign bias in international asset allocation. *Journal of Banking & Finance* 34(9), pp. 2121-2131.

Bhagat, S. and Black, B. 2001. The non-correlation between board independence and long-term firm performance. *Journal of Corporation Law* 27, pp. 231–273.

Bhatt, P.R. and Bhatt, R.R. 2017. Corporate governance and firm performance in Malaysia. *Corporate Governance* 17(5), pp. 896-912

Boisso, D. and Ferrantino, M. 1997. Economic distance, cultural distance, and openness in international trade: Empirical puzzles. *Journal of Economic Integration* 12(4), pp. 456-484.

Boivie, S. et al. 2016. Are boards designed to fail? The implausibility of effective board monitoring. *Academy of Management Annals* 10(1), pp. 319-407.

Boone, A.L. et al. 2007. The determinants of corporate board size and composition: An empirical analysis. *Journal of Financial Economics* 85(1), pp. 66-101.

Boubakri, N. and Saffar, W. 2016. Culture and externally financed firm growth. *Journal of Corporate Finance* 41, pp. 502-520.

Boubakri, N. et al. 2008. Political connections of newly privatized firms. *Journal of Corporate Finance* 14(5), pp. 654-673.

Bourdieu, P. 1986. The forms of capital. In: Richardson, J. ed. *Handbook of theory and research for the sociology of education*. Westport, CT: Greenwood, pp. 241-58.

Boyd, B. 1990. Corporate linkages and organizational environment: A test of the resource dependence model. *Strategic Management Journal* 11(6), pp. 419-430.

Boyd, B.K. 1995. CEO duality and firm performance: A contingency model. *Strategic Management Journal* 16(4), pp. 301-312.

Boyd, B.K. et al. 2011. Dimensions of CEO–board relations. *Journal of Management Studies* 48(8), pp. 1892-1923.

Brown, G.K. 2007. Making ethnic citizens: The politics and practice of education in Malaysia. *International Journal of Educational Development* 27(3), pp. 318-330.

Buck, T. and Shahrim, A. 2005. The translation of corporate governance changes across national cultures: The case of Germany. *Journal of International Business Studies* 36(1), pp. 42-61.

Burgstahler, D. and Dichev, I. 1997. Earnings management to avoid earnings decreases and losses. *Journal of Accounting and Economics* 24(1), pp. 99-126.

Burns, N. and Kedia, S. 2006. The impact of performance-based compensation on misreporting. *Journal of Financial Economics* 79(1), pp. 35-67.

Burt, R.S. 2000. The network structure of social capital. *Research in Organizational Behavior* 22, pp. 345-423.

Brechwald, W.A. and Prinstein, M.J. 2011. Beyond homophily: A decade of advances in understanding peer influence processes. *Journal of Research on Adolescence* 21(1), pp. 166-179.

Brewer, M.B. 1999. The psychology of prejudice: Ingroup love and outgroup hate? *Journal of Social Issues* 55(3), pp. 429-444.

Brewer, M.B. and Brown, R.J. 1998. Intergroup relations. In: Gilbert, D.T., Fiske, S.T., Lindzey, G. eds. *The handbook of social psychology*. 4th ed. Boston, MA: McGraw-Hill, pp. 554–594.

Brick, I.E. and Chidambaran, N.K. 2010. Board meetings, committee structure, and firm value. *Journal of Corporate Finance* 16(4), pp. 533-553.

Brickley, J.A. 2003. Empirical research on CEO turnover and firm-performance: A discussion. *Journal of Accounting and Economics* 36(1-3), pp. 227-233.

Brunello, G. et al. 2003. CEO turnover in insider-dominated boards: The Italian case. *Journal of Banking & Finance* 27(6), pp. 1027-1051.

Bruynseels, L. and Cardinaels, E. 2014. The audit committee: Management watchdog or personal friend of the CEO? *The Accounting Review* 89(1), pp. 113-145.

Bryan, S. et al. 2015. The effect of cultural distance on contracting decisions: The case of executive compensation. *Journal of Corporate Finance* 33, pp. 180-195.

Byrne, D. 1971. *The Attraction Paradigm*. New York: Academic Press.

Byrne, D. 1997. An overview (and underview) of research and theory within the attraction paradigm. *Journal of Social and Personal Relationships* 14(3), pp. 417-431.

Cai, Y. et al. 2019. Tone at the top: CEOs' religious beliefs and earnings management. *Journal of Banking & Finance* 106, pp. 195-213.

Calomiris, C.W. 1998. Blueprints for a new global financial architecture. In: Auenheimer, L. ed. *International financial markets: The challenge of globalization*. Chicago, Il: University of Chicago Press, pp. 259.

Cao, Y. et al. 2015. Are all independent directors equally informed? Evidence based on their trading returns and social networks. *Management Science* 61(4), pp. 795-813.

Carcello, J.V. et al. 2002. Board characteristics and audit fees. *Contemporary Accounting Research* 19(3), pp. 365-384.

Carrasco, A. et al. 2015. Appointing women to boards: Is there a cultural bias? *Journal of Business Ethics* 129(2), pp. 429-444.

Carter, D.A. et al. 2003. Corporate governance, board diversity, and firm value. *Financial review*, *38*(1), pp.33-53.

Casciaro, T. and Piskorski, M.J. 2005. Power imbalance, mutual dependence, and constraint absorption: A closer look at resource dependence theory. *Administrative Science Quarterly* 50(2), pp. 167-199.

Casey-Cannon, S.L. et al. 2011. Three ethnic and racial identity measures: Concurrent and divergent validity for diverse adolescents. *Identity: An International Journal of Theory and Research* 11(1), pp. 64-91.

Chahine, S. and Goergen, M. 2014. Top management ties with board members: How they affect pay–performance sensitivity and IPO performance. *Journal of Corporate Finance* 27, pp. 99-115.

Chakravarthy, B.S. 1986. Measuring strategic performance. *Strategic Management Journal* 7(5), pp. 437-458.

Chan, A.W. and Cheung, H.Y. 2012. Cultural dimensions, ethical sensitivity, and corporate governance. *Journal of Business Ethics* 110(1), pp. 45-59.

Cheah, B. K. 2009. Race and ethnic relations in colonial Malaya during the 1920s and 1930s. In: T. G. Lim, A. Gomes & A. Rahman. eds. *Multiethnic Malaysia: Past, Present and Future.* Malaysia: SIRD and MiDAS@UCSI University, pp. 33-44.

Chen, G. et al. 2016. Female board representation and corporate acquisition intensity. *Strategic Management Journal* 37(2), pp. 303-313.

Chen, X. et al. 2013. Family ownership and CEO turnovers. *Contemporary Accounting Research* 30(3), pp. 1166-1190.

Chen, X. et al. 2015. Does increased board independence reduce earnings management? Evidence from recent regulatory reforms. *Review of Accounting Studies* 20(2), pp. 899-933.

Cheng, Q. and Warfield, T.D. 2005. Equity incentives and earnings management. *The Accounting Review* 80(2), pp. 441-476.

Cheng, Q. et al. 2016. Internal governance and real earnings management. *The Accounting Review* 91(4), pp. 1051-1085.

Cheong, C.W. and Sinnakkannu, J. 2014. Ethnic diversity and firm financial performance: Evidence from Malaysia. *Journal of Asia-Pacific Business* 15(1), pp. 73-100.

Cheong, K.C. et al. 2009. Counting ethnicity: The national economic policy and social integration. *Malaysian Journal of Economic Studies* 46**,** pp**.** 33-52.

Cheong, S. 1993. *Bumiputera companies in the KLSE*. 2nd ed. Petaling Jaya, Malaysia: Corporate Research Services.

Child, J. and Möllering, G. 2003. Contextual confidence and active trust development in the Chinese business environment. *Organization Science* 14(1), pp. 69-80.

Chiu, P.C. et al. 2013. Board interlocks and earnings management contagion. *The Accounting Review* 88(3), pp. 915-944.

Chui, A.C. et al. 2010. Individualism and momentum around the world. *The Journal of Finance* 65(1), pp. 361-392.

Chung, R. et al. 2002. Institutional monitoring and opportunistic earnings management. *Journal of Corporate Finance* 8(1), pp. 29-48.

Clement, M.B. et al. 2003. The influence of culture and corporate governance on the characteristics that distinguish superior analysts. *Journal of Accounting, Auditing & Finance* 18(4), pp. 593-618.

Cohen, D.A. and Zarowin, P. 2010. Accrual-based and real earnings management activities around seasoned equity offerings. *Journal of Accounting and Economics* 50(1), pp. 2-19.

Cohen, D.A. et al. 2008. Real and accrual-based earnings management in the pre-and post-Sarbanes-Oxley periods. *The Accounting Review* 83(3), pp. 757-787.

Cokley, K. 2007. Critical issues in the measurement of ethnic and racial identity: A referendum on the state of the field. *Journal of Counseling Psychology* 54(3), p. 224.

Coles, J.L. et al. 2008. Boards: Does one size fit all? *Journal of Financial Economics* 87(2), pp. 329-356.

Coles, J.L. et al. 2014. Co-opted boards. *The Review of Financial Studies* 27(6), pp. 1751-1796.

Combs, J.G., Ketchen Jr, D.J., Perryman, A.A. and Donahue, M.S., 2007. The moderating effect of CEO power on the board composition–firm performance relationship. *Journal of management studies*, *44*(8), pp.1299-1323.

Core, J.E. et al. 1999. Corporate governance, chief executive officer compensation, and firm performance. *Journal of Financial Economics* 51(3), pp. 371-406.

Cornett, M.M. et al. 2009. Corporate governance and earnings management at large US bank holding companies. *Journal of Corporate Finance* 15(4), pp. 412-430.

Coughlan, A.T. and Schmidt, R.M. 1985. Executive compensation, management turnover, and firm performance: An empirical investigation. *Journal of Accounting and Economics* 7(1-3), pp. 43-66.

Cox, T.H. et al. 1991. Effects of ethnic group cultural differences on cooperative and competitive behavior on a group task. *Academy of Management Journal* 34(4), pp. 827-847.

Cragg, J.G. and Donald, S.G. 1993. Testing identifiability and specification in instrumental variable models. *Econometric Theory* 9(2), pp. 222-240.

Craig, C.S. and Douglas, S.P. 2006. Beyond national culture: implications of cultural dynamics for consumer research. *International Marketing Review* 23(3), pp. 322-342

Crouch, H. 2001. Managing ethnic tensions through affirmative action: The Malaysian experience. *Social Cohesion and Conflict in Asia*, pp. 225-262.

Dahlan, H.M. 1991. Local values in intercultural management. *Malaysian Management Review* 1, pp. 45-50.

Dah, M.A. et al. 2014. Board changes and CEO turnover: The unanticipated effects of the Sarbanes–Oxley Act. *Journal of Banking & Finance* 41, pp. 97-108.

Dahya, J. et al. 2002. The Cadbury committee, corporate performance, and top management turnover. *The Journal of Finance* 57(1), pp. 461-483.

Dahya, J. et al. 2008. Dominant shareholders, corporate boards, and corporate value: A cross-country analysis. *Journal of Financial Economics* 87(1), pp. 73-100.

Daily, C.M. and Dalton, D.R. 1994. Bankruptcy and corporate governance: The impact of board composition and structure. *Academy of Management Journal* 37(6), pp. 1603-1617.

Dalton, D.R. et al. 1998. Meta-analytic reviews of board composition, leadership structure, and financial performance. *Strategic Management Journal* 19(3), pp. 269-290.

Dalton, D.R. et al. 2003. Meta-analyses of financial performance and equity: fusion or confusion? *Academy of Management Journal* 46(1), pp. 13-26.

Dalton, D.R. et al. 2007. The fundamental agency problem and its mitigation. *Academy of Management Annals* 1(1), pp. 1-64.

Daniel, S.J. et al. 2012. The impact of national economic culture and country-level institutional environment on corporate governance practices. *Management International Review* 52(3), pp. 365-394.

Daniels, T. P. 2005. *Building cultural nationalism in Malaysia: identity, representation, and citizenship.* 1st ed. New York, NY: Routledge.

Dechow, P.M. et al. 1995. Detecting earnings management. *Accounting Review* 70(2), pp. 193-225.

Dechow, P.M. et al. 2012. Detecting earnings management: A new approach. *Journal of Accounting Research* 50(2), pp. 275-334.

Deephouse, D.L. and Jaskiewicz, P. 2013. Do family firms have better reputations than non-family firms? An integration of socioemotional wealth and social identity theories. *Journal of Management Studies* 50(3), pp. 337-360.

DeFond, M.L. et al. 2005. Does the market value financial expertise on audit committees of boards of directors? *Journal of Accounting Research* 43(2), pp. 153-193.

DeFond, M.L. and Jiambalvo, J. 1994. Debt covenant violation and manipulation of accruals. *Journal of Accounting and Economics* 17(1-2), pp. 145-176.

DeFond, M.L. and Park, C.W. 1997. Smoothing income in anticipation of future earnings. *Journal of Accounting and Economics* 23(2), pp. 115-139.

DeFond, M.L. and Park, C.W. 1999. The effect of competition on CEO turnover. *Journal of Accounting and Economics* 27(1), pp. 35-56.

Degeorge, F. et al. 1999. Earnings management to exceed thresholds. *The Journal of Business* 72(1), pp. 1-33.

Dehejia, R.H. and Wahba, S. 2002. Propensity score-matching methods for nonexperimental causal studies. *Review of Economics and Statistics* 84(1), pp. 151-161.

Denis, D.J. et al. 2006. Is there a dark side to incentive compensation? *Journal of Corporate Finance* 12(3), pp. 467-488.

Department of Statistics Malaysia. 2016. *Current population estimates Malaysia 2014-2016*, Available at: https://www.dosm.gov.my/v1/index.php?r=column/cthemeByCat&cat=155&bul_id=OWlxdEVoYlJCS0hUZzJyRUcvZEYxZz09&menu_id=L0pheU43NWJwRWVSZklWdzQ4TlhUUT09. [Accessed at 5 January 2021]

Deschamps, J.C. and Brown, R. 1983. Superordinate goals and intergroup conflict. *British Journal of Social Psychology* 22(3), pp. 189-195.

Desmet, K. et al. 2017. Culture, ethnicity, and diversity. *American Economic Review* 107(9), pp. 2479-2513.

Dey, A. and Liu, X. 2010. Social connections, stock-based compensation, and director oversight. SSRN. Available at: https://papers.ssrn.com/sol3/Delivery.cfm?delivery_id=1581212

Dikolli, S.S. et al. 2014. CEO tenure and the performance-turnover relation. *Review of Accounting Studies* 19(1), pp. 281-327.

Doidge, C. et al. 2007. Why do countries matter so much for corporate governance? *Journal of Financial Economics* 86(1), pp. 1-39.

Doraisami, A. 2012. Economic crisis and policy response in Malaysia: the role of the new economic policy. *Asian-Pacific Economic Literature* 26(2), pp. 41-53.

Drees, J.M. and Heugens, P.P. 2013. Synthesizing and extending resource dependence theory: A meta-analysis. *Journal of Management* 39(6), pp. 1666-1698.

DuCharme, L.L. et al. 2004. Earnings management, stock issues, and shareholder lawsuits. *Journal of Financial Economics* 71(1), pp. 27-49.

Duong, H.K. et al. 2016. National culture and corporate governance. *Journal of International Accounting Research* 15(3), pp. 67-96.

Earle, T.C. and Cvetkovich, G. 1995. *Social trust: Toward a cosmopolitan society*. Westport, CT: Praeger Publishers.

Eisenhardt, K.M. 1989. Agency theory: An assessment and review. *Academy of Management Review* 14(1), pp. 57-74.

El Ghoul, S. and Zheng, X. 2016. Trade credit provision and national culture. *Journal of Corporate Finance* 41, pp. 475-501.

Elkins, Z. and Sides, J. 2007. Can institutions build unity in multiethnic states? *American Political Science Review* 101(4), pp. 693-708.

Encyclopaedia Britannica, Inc. 2009. *Map of Malaysia.*
Available at: https://www.britannica.com/place/Malaysia. [Accessed: 3 August 2020]

Eun, C.S. et al. 2015. Culture and R2. *Journal of Financial Economics* 115(2), pp. 283-303.

EPU – Economic Planning Unit. 1971. *Second Malaysia plan, 1971-1975.* Available at: http://www.epu.gov.my/en/rmk/second-malaysia-plan-1971-1975. [Accessed: 3 August 2020]

EPU – Economic Planning Unit. 1976. *Third Malaysia plan, 1976–1980.* Available at: http://www.epu.gov.my/en/rmk/third-malaysia-plan-1976-1980. [Accessed: 3 August 2020]

EPU – Economic Planning Unit. 1981. *Fourth Malaysia plan, 1981–1985.* Available at: http://www.epu.gov.my/en/rmk/fourth-malaysia-plan-1981-1985. [Accessed: 3 August 2020]

EPU – Economic Planning Unit. 1986. *Fifth Malaysia plan, 1986–1990.* Available at: http://www.epu.gov.my/en/rmk/fifth-malaysia-plan-1986-1990. [Accessed: 3 August 2020]

EPU – Economic Planning Unit. 1990. *Sixth Malaysia plan, 1990–1995.* Available at: http://www.epu.gov.my/en/rmk/sixth-malaysia-plan-1990-1995. [Accessed: 3 August 2020]

EPU – Economic Planning Unit. 1996. *Seventh Malaysia plan, 1996–2000.* Available at: http://www.epu.gov.my/en/rmk/seventh-malaysia-plan-1996-2000. [Accessed: 3 August 2020]

EPU – Economic Planning Unit. 2006. *Ninth Malaysia plan, 2006–2010*. Available at: http://www.epu.gov.my/en/rmk/ninth-malaysia-plan-2006-2010. [Accessed: 3 August 2020]

EPU – Economic Planning Unit. 2011. *Tenth Malaysia plan, 2011–2015.* Available at: http://www.epu.gov.my/en/rmk/tenth-malaysia-plan-2011-2015. [Accessed: 3 August 2020]

EPU – Economic Planning Unit. 2015. *Eleventh Malaysia plan, 2016–2020.* Available at: http://www.epu.gov.my/en/rmk/eleventh-malaysia-plan-2016-2020. [Accessed: 3 August 2020]

Erhardt, N.L. et al. 2003. Board of director diversity and firm financial performance. *Corporate Governance: An international Review, 11*(2), pp.102-111.

Evans, J.H. et al. 2014. CEO turnover, financial distress, and contractual innovations. *The Accounting Review* 89(3), pp. 959-990.

Faccio, M. 2006. Politically connected firms. *American Economic Review* 96(1), pp. 369-386.

Faleye, O. 2015. The costs of a (nearly) fully independent board. *Journal of Empirical Finance* 32, pp. 49-62.

Faleye, O. et al. 2011. The costs of intense board monitoring. *Journal of Financial Economics* 101(1), pp. 160-181.

Faleye, O. et al. 2014. Do better-connected CEOs innovate more? *Journal of Financial and Quantitative Analysis* 49(5-6), pp. 1201-1225.

Fama, E.F., 1980. Agency problems and the theory of the firm. *Journal of Political Economy* 88(2), pp. 288-307.

Fama, E.F. and Jensen, M.C. 1983. Separation of ownership and control. *The Journal of Law and Economics* 26(2), pp. 301-325.

Fan, J.P. et al. 2007. Politically connected CEOs, corporate governance, and Post-IPO performance of China's newly partially privatized firms. *Journal of Financial Economics* 84(2), pp. 330-357.

Fan, Y. et al. 2019. Board-CEO friendship ties and firm value: Evidence from US firms. *International Review of Financial Analysis* 65, pp. 101373.

Fauzi, F. and Locke, S. 2012. Board structure, ownership structure and firm performance: A study of New Zealand listed-firms. *Asian Academy of Management Journal of Accounting and Finance* 8(2), pp. 43–67

Firth, M. et al. 2006. Firm performance, governance structure, and top management turnover in a transitional economy. *Journal of Management Studies* 43(6), pp. 1289-1330.

Fisman, R. et al. 2017. Cultural proximity and loan outcomes. *American Economic Review* 107(2), pp .457-92.

Flannery, M.J. and Rangan, K.P. 2006. Partial adjustment toward target capital structures. *Journal of Financial Economics* 79(3), pp. 469-506.

Fontaine, R. and Richardson, S. 2005. Cultural values in Malaysia: Chinese, Malays and Indians compared. *Cross Cultural Management: An International Journal* 12(4), pp. 63-77

Forbes, D.P. and Milliken, F.J. 1999. Cognition and corporate governance: Understanding boards of directors as strategic decision-making groups. *Academy of Management Review* 24(3), pp. 489-505.

Fracassi, C. and Tate, G. 2012. External networking and internal firm governance. *The Journal of Finance* 67(1), pp. 153-194.

Francis, B. et al. 2015. Gender differences in financial reporting decision making: Evidence from accounting conservatism. *Contemporary Accounting Research* 32(3), pp. 1285-1318.

Franz, D.R. et al. 2014. Impact of proximity to debt covenant violation on earnings management. *Review of Accounting Studies* 19(1), pp. 473-505.

Frijns, B. et al. 2016. The impact of cultural diversity in corporate boards on firm performance. *Journal of Corporate Finance* 41, pp.521-541.

Frydman, C. and Jenter, D. 2010. CEO compensation. *Annual Review of Financial Economics.* 2, pp. 75-102.

Gabriel, S.P. 2015. The meaning of race in Malaysia: Colonial, post-colonial and possible new conjunctures. *Ethnicities* 15(6), pp. 782-809.

Gabrielsson, J. and Winlund, H. 2000. Boards of directors in small and medium-sized industrial firms: examining the effects of the board's working style on board task performance. *Entrepreneurship & Regional Development* 12(4), pp. 311-330.

Gale, B. 1982. *Musa Hitam: A political biography.* Petaling Jaya, Malaysia: Eastern Universities Press.

Gentry, R.J. and Shen, W. 2010. The relationship between accounting and market measures of firm financial performance: How strong is it? *Journal of Managerial Issues* 22(4), pp. 514-530.

Giannetti, M. and Yafeh, Y. 2012. Do cultural differences between contracting parties matter? Evidence from syndicated bank loans. *Management Science 58*(2), pp. 365-383.

Gibson, M.S. 2003. Is corporate governance ineffective in emerging markets? *Journal of Financial and Quantitative Analysis* 38(1), pp. 231-250.

Goergen, M. et al. 2015. Mind the gap: The age dissimilarity between the chair and the CEO. *Journal of Corporate Finance* 35, pp. 136-158.

Goldman, E. et al. 2009. Do politically connected boards affect firm value? *The Review of Financial Studies* 22(6), pp. 2331-2360.

Gomez, E.T. 2002. Political business in Malaysia: party factionalism, corporate development, and economic crisis, In: Gomez E., T. ed. *Political business in East Asia*. London: Routledge, pp. 82-113

Gomez, E.T. et al. 1999. *Malaysia's political economy: Politics, patronage and profits*. Cambridge, UK: CUP Archive.

Gompers, P.A. et al. 2016. The cost of friendship. *Journal of Financial Economics* 119(3), pp. 626-644.

Gomulya, D. and Boeker, W. 2014. How firms respond to financial restatement: CEO successors and external reactions. *Academy of Management Journal* 57(6), pp. 1759-1785.

Gore, J. and Pepper, A. 2012. Taking stock of long-term incentive plans: Effective and efficient ways of motivating senior executives. In *Executive Remuneration Conference, 2012*. Available at: http://docs.business.auckland.ac.nz/Doc/Gore-Pepper-Auckland-13th-Aug-2012.pdf.

Goyal, V.K. and Park, C.W. 2002. Board leadership structure and CEO turnover. *Journal of Corporate Finance* 8(1), pp. 49-66.

Graham, J.R. et al. 2005. The economic implications of corporate financial reporting. *Journal of Accounting and Economics* 40(1-3), pp. 3-73.

Griffin, D. et al. 2017a. National culture: The missing country-level determinant of corporate governance. *Journal of International Business Studies* 48(6), pp. 740-762.

Griffin, D.W. et al. 2017b. National culture and the value implication of corporate governance. Available at:
SSRN https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2400078.

Grinblatt, M. and Keloharju, M. 2001. How distance, language, and culture influence stockholdings and trades. *The Journal of Finance* 56(3), pp. 1053-1073.

Guiso, L. et al. 2006. Does culture affect economic outcomes? *Journal of Economic Perspectives* 20(2), pp. 23-48.

Guiso, L. et al. 2009. Cultural biases in economic exchange? *The Quarterly Journal of Economics* 124(3), pp. 1095-1131.

Guiso, L. et al. 2015. Corporate culture, societal culture, and institutions. *American Economic Review* 105(5), pp. 336-39.

Gul, F.A. et al. 2016. Ethnicity, politics and firm performance: Evidence from Malaysia. *Pacific-Basin Finance Journal* 40, pp. 115-129.

Gunny, K.A. 2010. The relation between earnings management using real activities manipulation and future performance: Evidence from meeting earnings benchmarks. *Contemporary Accounting Research* 27(3), pp. 855-888.

Haggard, S. 2000. *The political economy of the Asian financial crisis*. Washington, DC: Institute for International Economics.

Hair, J.F. et al. 1998. *Multivariate data analysis*. Upper Saddle River, NJ: Prentice Hall.

Haniffa, R.M. and Cooke, T.E. 2002. Culture, corporate governance and disclosure in Malaysian corporations. *Abacus* 38(3), pp. 317-349.

Haniffa, R.M. and Cooke, T.E. 2005. The impact of culture and governance on corporate social reporting. *Journal of Accounting and Public Policy* 24(5), pp. 391-430.

Hansen, L.P. 1982. Large sample properties of generalized method of moments estimators. *Econometrica: Journal of the Econometric Society* 50(4), pp. 1029-1054.

Haque, M.S. 2003. The role of the state in managing ethnic tensions in Malaysia: A critical discourse. *American Behavioral Scientist* 47(3), pp. 240-266.

Hassan, R. and Marimuthu, M. 2018. Contextualizing comprehensive board diversity and firm financial performance: Integrating market, management and shareholder's perspective. *Journal of Management and Organization* 24(5), pp. 634-678.

Hazarika, S. et al. 2012. Internal corporate governance, CEO turnover, and earnings management. *Journal of Financial Economics* 104(1), pp. 44-69.

Healy, P.M., 1985. The effect of bonus schemes on accounting decisions. *Journal of Accounting and Economics* 7(1-3), pp. 85-107.

Healy, P.M. and Wahlen, J.M. 1999. A review of the earnings management literature and its implications for standard setting. *Accounting Horizons* 13(4), pp. 365-383.

Hegde, D. and Tumlinson, J. 2012. Can birds of a feather fly together? Evidence for the economic payoffs of ethnic homophily. *Academy of Management Proceedings* 1, pp. 1329.

He, G. 2016. Fiscal support and earnings management. *The International Journal of Accounting* 51(1), pp. 57-84.

He, L. et al. 2009. Board monitoring, audit committee effectiveness, and financial reporting quality: review and synthesis of empirical evidence. *Journal of Forensic & Investigative Accounting, 1*(2), Available at:
SSRN https://ssrn.com/abstract=1159453

Hermalin, B.E. and Weisbach, M.S. 2003. Boards of directors as an endogenously determined institution: a survey of the economic literature. *Economic Policy Review* 9, pp. 7–26.

Hewstone, M. et al. 2002. Intergroup bias. *Annual Review of Psychology* 53(1), pp. 575-604.

Higginbotham, E. and Anderson, M.L. 2012. The Social Construction of Race and Ethnicity. *Race and Ethnicity in Society: The Changing Landscape*, pp. 3-6.

Hillman, A. J., and Dalziel, T. 2003. Boards of directors and firm performance: Integrating agency and resource dependence perspectives. *Academy of Management Review* 28(3), pp. 383-396.

Hillman, A.J. et al. 2008. Directors' multiple identities, identification, and board monitoring and resource provision. *Organization Science* 19(3), pp. 441-456.

Hillman, A.J. et al. 2009. Resource dependence theory: A review. *Journal of Management* 35(6), pp. 1404-1427.

Hirschman, C. 1986. The making of race in colonial Malaya: Political economy and racial ideology. *Sociological Forum* 1(2), pp. 330-361

Ho, J.A. 2010. Ethical perception: are differences between ethnic groups situation dependent? *Business Ethics: A European Review* 19(2), pp. 154-182.

Hofstede, G. 1984. *Culture's consequences: International differences in work-related values*. London and Beverly Hills, CA: Sage Publications.

Hofstede, G. 1991. *Cultures and organizations: Software of the mind*. London: McGraw-Hill Publishers.

Hofstede, G. 1998. Attitudes, values and organizational culture: Disentangling the concepts. *Organization Studies* 19(3), pp. 477-493.

Hofstede, G. 2001. *Culture's consequences: Comparing values, behaviors, institutions and organizations across nations*. Thousand Oaks, CA: Sage Publications.

Hogg, M. A. 2006. Social identity theory. In: Burke P., J. ed. *Contemporary social psychological theories*. Stanford, CA: Stanford University Press, pp. 111–136.

Hogg, M.A. and Terry, D.I. 2000. Social identity and self-categorization processes in organizational contexts. *Academy of Management Review* 25(1), pp. 121-140.

Hoitash, U. 2011. Should independent board members with social ties to management disqualify themselves from serving on the board? *Journal of Business Ethics* 99(3), pp. 399-423.

Holderness, C.G. 2017. Culture and the ownership concentration of public corporations around the world. *Journal of Corporate Finance* 44, pp. 469-486.

Horton, J. et al. 2012. Resources or power? Implications of social networks on compensation and firm performance. *Journal of Business Finance & Accounting* 39(3-4), pp. 399-426.

Horwitz, M. and Rabbie, J.M. 1982. Individuality and membership in the intergroup system. *Social Identity and Intergroup Relations*, pp. 241-274.

House, R.J. et al. 2004. *Culture, leadership, and organizations: The GLOBE study of 62 societies*. Thousand Oaks, CA: Sage Publications.

Hribar, P. and Craig Nichols, D. 2007. The use of unsigned earnings quality measures in tests of earnings management. *Journal of Accounting Research* 45(5), pp. 1017-1053.

Hsieh, T.S. et al. 2014. CEO overconfidence and earnings management during shifting regulatory regimes. *Journal of Business Finance & Accounting* 41(9-10), pp. 1243-1268.

Huddy, L. 2001. From social to political identity: A critical examination of social identity theory. *Political Psychology* 22(1), pp. 127-156.

Humphries, S.A. and Whelan, C. 2017. National culture and corporate governance codes. *Corporate Governance: The International Journal of Business in Society* 17(1), pp. 152-163

Huson, M.R. et al. 2001. Internal monitoring mechanisms and CEO turnover: A long-term perspective. *the Journal of Finance* 56(6), pp. 2265-2297.

Huson, M.R. et al. 2004. Managerial succession and firm performance. *Journal of Financial Economics* 74(2), pp. 237-275.

Hwang, B.H. and Kim, S. 2009. It pays to have friends. *Journal of Financial Economics* 93(1), pp. 138-158.

Hwang, B.H. and Kim, S. 2012. Social ties and earnings management.
Available at: https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1215962

Ibrahim, R. et al. 2011. Multiculturalism and higher education in Malaysia. *Procedia-Social and Behavioral Sciences* 15, pp. 1003-1009.

Inkpen, A.C. and Tsang, E.W. 2005. Social capital, networks, and knowledge transfer. *Academy of Management Review* 30(1), pp. 146-165.

Jacobs, J.B. 1979. A preliminary model of particularistic ties in Chinese political alliances: Kan-ch'ing and Kuan-hsi in a rural Taiwanese township. *China Quarterly* 78, pp. 237-273.

Jalil, H. 2015. *Increase in equity ownership of Bumiputera and Indians*. The Sun Daily. Available at: http://www.thesundaily.my/news/1619531.

Jensen, M.C. 1993. The modern industrial revolution, exit, and the failure of internal control systems. *the Journal of Finance* 48(3), pp. 831-880.

Jensen, M.C. and Meckling, W.H. 1976. Theory of the firm: Managerial behavior, agency costs and ownership structure. *Journal of Financial Economics* 3(4), pp. 305-360.

Jensen, M.C. and Ruback, R.S. 1983. The market for corporate control: The scientific evidence. *Journal of Financial Economics* 11(1-4), pp. 5-50.

Jenter, D. and Lewellen, K. 2021. Performance-induced CEO turnover. *The Review of Financial Studies* 34(2), pp. 569-617.

Johnson, J.L. et al. 1996. Boards of directors: A review and research agenda. *Journal of Management* 22(3), pp. 409-438.

Johnson, S. and Mitton, T. 2003. Cronyism and capital controls: evidence from Malaysia. *Journal of Financial Economics* 67(2), pp. 351-382.

Jomo, K.S. 1990. Whither Malaysia's new economic policy? *Pacific Affairs* 63(4), pp. 469-499.

Kale, J.R. et al. 2009. Rank-order tournaments and incentive alignment: The effect on firm performance. *The Journal of Finance* 64(3), pp. 1479-1512.

Kandel, D.B. 1978. Homophily, selection, and socialization in adolescent friendships. *American Journal of Sociology* 84(2), pp. 427-436.

Kang, J.K. et al. 2018. Friendly boards and innovation. *Journal of Empirical Finance* 45, pp. 1-25.

Kaplan, S.N. and Minton, B.A. 2012. How has CEO turnover changed? *International Review of Finance* 12(1), pp. 57-87.

Karolyi, G.A. 2016. The gravity of culture for finance. *Journal of Corporate Finance* 41, pp. 610-625.

Katmon, N. et al. 2019. Comprehensive board diversity and quality of corporate social responsibility disclosure: evidence from an emerging market. *Journal of Business Ethics* 157(2), pp. 447-481.

Kasznik, R. 1999. On the association between voluntary disclosure and earnings management. *Journal of Accounting Research* 37(1), pp. 57-81.

Kennedy, P. 1998. *A guide to econometrics*. 4th ed. Malden, MA: Blackwell Publishers

Khanna, V. et al. 2015. CEO connectedness and corporate fraud. *The Journal of Finance* 70(3), pp. 1203-1252.

Khedmati, M. et al. 2020. CEO-director ties and labor investment efficiency. *Journal of Corporate Finance* 65, pp. 101492.

Khoo, K. K. 2009. The emergence of plural communities in the Malay peninsula before 1874. In: T. G. Lim, A. Gomes & A. Rahman. Eds. *Multiethnic Malaysia: Past, Present and Future*. Malaysia: SIRD and MiDAS@UCSI University, pp. 11-32

Khwaja, A.I. and Mian, A. 2005. Do lenders favor politically connected firms? Rent provision in an emerging financial market. *The Quarterly Journal of Economics* 120(4), pp. 1371-1411.

Kia Soong, K. 1987. *Polarization in Malaysia: The root causes.* Kuala Lumpur, Malaysia: Malaysian Chinese Research and Resource Center.

Kim, J.B. and Sohn, B.C. 2013. Real earnings management and cost of capital. *Journal of Accounting and Public Policy* 32(6), pp. 518-543.

Kim, J. et al. 2017. Languages and earnings management. *Journal of Accounting and Economics* 63(2-3), pp. 288-306.

Kish-Gephart, J.J. and Campbell, J.T. 2015. You don't forget your roots: The influence of CEO social class background on strategic risk taking. *Academy of Management Journal* 58(6), pp. 1614-1636.

Klein, A. 2002. Audit committee, board of director characteristics, and earnings management. *Journal of Accounting and Economics* 33(3), pp. 375-400.

Kolb, R.W. 2010. *Lessons from the financial crisis: Causes, consequences, and our economic future*. Hoboken, NJ; John Wiley & Sons.

Kong, D. et al. 2020. CEOs' hometown connections and access to trade credit: Evidence from China. *Journal of Corporate Finance* 62, p. 101574.

Kothari, S.P. et al. 2016. Managing for the moment: The role of earnings management via real activities versus accruals in SEO valuation. *The Accounting Review* 91(2), pp. 559-586.

Kramarz, F. and Thesmar, D. 2013. Social networks in the boardroom. *Journal of the European Economic Association* 11(4), pp. 780-807.

Krishnan, G.V. et al. 2011. CFO/CEO-board social ties, Sarbanes-Oxley, and earnings management. *Accounting Horizons* 25(3), pp. 537-557.

Krishnan, G.V. and Visvanathan, G. 2007. Does the SOX definition of an accounting expert matter? The association between audit committee directors' accounting expertise and accounting conservatism. Available at:

https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1029752

Kuang, Y.F. et al. 2014. CEO origin and accrual-based earnings management. *Accounting Horizons* 28(3), pp. 605-626.

Larcker, D.F. et al. 2007. Corporate governance, accounting outcomes, and organizational performance. *The Accounting Review* 82(4), pp. 963-1008.

Laux, V. 2008. Board independence and CEO turnover. *Journal of Accounting Research* 46(1), pp. 137-171.

Langenberg, E.A. 2007. *Guanxi and business strategy: Theory and implications for multinational companies in China*. Berlin, Germany: Springer Science & Business Media.

Langevoort, D.C. 2007. The social construction of Sarbanes-Oxley. *Michigan Law Review* 105(8), pp. 1817-1855.

Lazarsfeld, P.F. and Merton, R.K. 1954. Friendship as a social process: A substantive and methodological analysis. *Freedom and Control in Modern Society* 18(1), pp. 18-66

Lee, C. et al. 2001. Internal capabilities, external networks, and performance: a study on technology-based ventures. *Strategic Management Journal* 22(6-7), pp. 615-640

Lee, J. et al. 2014. Birds of a feather: Value implications of political alignment between top management and directors. *Journal of Financial Economics* 112(2), pp. 232-250.

Lee, Y.T. 1993. Ingroup preference and homogeneity among African American and Chinese American students. *The Journal of Social Psychology* 133(2), pp. 225-235.

Leszczensky, L. and Pink, S. 2015. Ethnic segregation of friendship networks in school: Testing a rational-choice argument of differences in ethnic homophily between classroom-and grade-level networks. *Social Networks* 42, pp. 18-26.

Leszczensky, L. and Pink, S. 2019. What drives ethnic homophily? A relational approach on how ethnic identification moderates preferences for same-ethnic friends. *American Sociological Review* 84(3), pp. 394-419

Leuz, C. et al. 2003. Earnings management and investor protection: an international comparison. *Journal of Financial Economics* 69(3), pp. 505-527.

Lievenbrück, M. and Schmid, T. 2014. Why do firms (not) hedge?—Novel evidence on cultural influence. *Journal of Corporate Finance* 25, pp. 92-106.

Li, J. and Harrison, J.R. 2008a. Corporate governance and national culture: a multi-country study. *Corporate Governance: The International Journal of Business in Society* 8(5), pp. 607-621

Li, J. and Harrison, J.R. 2008b. National culture and the composition and leadership structure of boards of directors. *Corporate Governance: An International Review* 16(5), pp. 375-385.

Li, K. et al. 2013. How does culture influence corporate risk-taking? *Journal of Corporate Finance* 23, pp. 1-22.

Lim, D.C. 2008. *Overcoming passion for race in Malaysia cultural studies*. Leiden, Holland: Brill.

Lim, J. et al. 2016. The asymmetric relationship between national cultural distance and target premiums in cross-border M&A. *Journal of Corporate Finance* 41, pp. 542-571.

Lim, L. 2001. Work-related values of Malays and Chinese Malaysians. *International Journal of Cross-Cultural Management* 1(2), pp. 209-226.

Lim, M. H. 1981. *Ownership and control of the one hundred largest corporations in Malaysia*. Oxford, UK: Oxford University Press.

Linck, J.S. et al. 2008. The determinants of board structure. *Journal of Financial Economics* 87(2), pp. 308-328.

Lin, N. et al. R.M. 2001. Measurement techniques for investigations of social capital. *Social Capital: Theory and Research*, pp. 57-81.

Ling, Y. et al. 2007. Influence of founder—CEOs' personal values on firm performance: Moderating effects of firm age and size. *Journal of Management* 33(5), pp. 673-696.

Little, D. 2012. Explanatory autonomy and Coleman's boat. *THEORIA Revista de Teoria, Historia y Fundamentos de la Ciencia* 27(2), pp. 137–151.

Liu, Y. 2014. Outside options and CEO turnover: The network effect. *Journal of Corporate Finance* 28, pp. 201-217.

Lorsch, J.W. and MacIver, E. 1989. *Pawns or potentates: The reality of America's corporate boards*. Boston, Mass: Harvard Business School Press.

Lubatkin, M. and Shrieves, R.E. 1986. Towards reconciliation of market performance measures to strategic management research. *Academy of Management Review* 11(3), pp. 497-512.

Luhtanen, R. and Crocker, J. 1992. A collective self-esteem scale: Self-evaluation of one's social identity. *Personality and Social Psychology Bulletin* 18(3), pp. 302-318.

Macey, J.R. 1998. Measuring the effectiveness of different corporate governance systems: toward a more scientific approach. *Bank of America Journal of Applied Corporate Finance* 63(2). Available at SSRN: https://ssrn.com/abstract=10596.

Mallette, P. and Fowler, K.L. 1992. Effects of board composition and stock ownership on the adoption of "poison pills". *Academy of Management journal* 35(5), pp. 1010-1035.

Maniam, M. 1986. The influence of culture in management in Malaysia. *Malaysian Management Review*, 21(3), pp. 3-7.

Mariappan, K. 2002. Ethnicity, Malay nationalism, and the question of bangsa Malaysia. In: Fenton S., May S. eds. *Ethnonational identities*. London: Palgrave Macmillan, pp. 198-226.

Marimuthu, M. and Kolandaisamy, I. 2009. Ethnic and gender diversity in boards of directors and their relevance to financial performance of Malaysian companies. *Journal of Sustainable Development* 2(3), pp. 139-148

Masson, C.N. and Verkuyten, M. 1993. Prejudice, ethnic identity, contact and ethnic group preferences among Dutch young adolescents. *Journal of Applied Social Psychology* 23(2), pp. 156-168.

Mateos, P. 2007. A review of name-based ethnicity classification methods and their potential in population studies. *Population, Space and Place* 13(4), pp. 243-263.

McLaren, M.C. and Rashid, M.Z.A. 2002. *Issues and cases in cross-cultural management: An Asian perspective*. Selangor, Malaysia: Prentice Hall (Pearson Education Malaysia Sdn. Bhd.).

McPherson, M. et al. 2001. Birds of a feather: Homophily in social networks. *Annual Review of Sociology* 27(1), pp. 415-444.

McSweeney, B. 2000. The fallacy of national culture identification.

Available at: http://www. les. man. ac. uk. *IPA/papers*.

McSweeney, B. 2002a. Hofstede's model of national cultural differences and their consequences: A triumph of faith-a failure of analysis. *Human Relations* 55(1), pp. 89-118.

McSweeney, B. 2002b. The essentials of scholarship: A reply to Geert Hofstede. *Human Relations* 55(11), pp. 1363-1372.

Melitz, J. 2008. Language and foreign trade. *European Economic Review* 52(4), pp. 667-699.

Melkumov, D. et al. 2015. Directors' social identifications and board tasks: Evidence from Finland. *Corporate Governance: An International Review* 23(1), pp. 42-59.

Meyer, J.W. and Rowan, B. 1977. Institutionalized organizations: Formal structure as myth and ceremony. *American Journal of Sociology* 83(2), pp. 340-363.

Michels, R. 1962. *Political Parties*. New York: Free Press

Milliken, F.J. and Martins, L.L., 1996. Searching for common threads: Understanding the multiple effects of diversity in organizational groups. *Academy of Management Review*, *21*(2), pp.402-433.

Mills, J. and Clark, M. S. 1982. Exchange and communal relationships. In L. Wheeler. ed. *Review of personality and social psychology*. 3rd ed. Beverly Hills, CA: Sage, pp. 121–144.

Mohamad-Yusof, N.Z. et al. 2018. Corporate governance, critical junctures and ethnic politics: Ownership and boards in Malaysia. *Critical Perspectives on Accounting* 55, pp. 33-52.

Montoya, R.M. et al. 2008. Is actual similarity necessary for attraction? A meta-analysis of actual and perceived similarity. *Journal of Social and Personal Relationships* 25(6), pp. 889-922.

Morrison, K.R. et al. 2009. Group status, perceptions of threat, and support for social inequality. *Journal of Experimental Social Psychology* 45(1), pp. 204-210.

Morrison, K.R. and Ybarra, O. 2009. Symbolic threat and social dominance among liberals and conservatives: SDO reflects conformity to political values. *European Journal of Social Psychology* 39(6), pp. 1039-1052.

Munusamy, V.P. 2012. Ethnic relations in Malaysia: the need for “constant repair” in the spirit of Muhibbah. In: Landis, D. and Albert. R. eds. *Handbook of ethnic conflict*. Boston, MA: Springer, pp. 119-136.

Myers, M.D. and Tan, F.B. 2002. Beyond models of national culture in information systems research. In: Coral, R. and Edward, J. eds. *Human factors in information systems.* United Kingdom: IGI Global, pp. 1-19.

Nahapiet, J. and Ghoshal, S. 1998. Social capital, intellectual capital, and the organizational advantage. *Academy of Management Review* 23(2), pp. 242-266.

Nagayoshi, K. 2011. Support of multiculturalism, but for whom? Effects of ethno-national identity on the endorsement of multiculturalism in Japan. *Journal of Ethnic and Migration Studies* 37(4), pp. 561-578.

Nederveen Pieterse, A. et al. 2013. Cultural diversity and team performance: The role of team member goal orientation. *Academy of Management Journal*, *56*(3), pp.782-804.

Neville, F. et al. 2019. Board independence and corporate misconduct: A cross-national meta-analysis. *Journal of Management*, 45(6), pp. 2538-2569.

Nguyen, B.D. 2012. Does the Rolodex matter? Corporate elite's small world and the effectiveness of boards of directors. *Management Science* 58(2), pp. 236-252.

Nguyen, D.D. et al. 2018. Does a CEO’s cultural heritage affect performance under competitive pressure? *The Review of Financial Studies* 31(1), pp. 97-141.
Ng Tseung-Wong, C. and Verkuyten, M. 2018. Diversity ideologies and intergroup attitudes: When multiculturalism is beneficial for majority group members. *Group Processes & Intergroup Relations* 21(2), pp. 336-350.

Nilsson, M. 2019. Proximity and the trust formation process. *European Planning Studies* 27(5), pp. 841-861.

Noor, N.M. 2007. Polarisation and inequality in Malaysia: The future of Malay-Chinese relations. *Intellectual Discourse* 15(2) pp. 191-204

Noor, N.M. and Leong, C.H. 2013. Multiculturalism in Malaysia and Singapore: Contesting models. *International Journal of Intercultural Relations* 37(6), pp. 714-726.

North, D. C. 1990. *Institutions, Institutional Change and Economic Performance*. New York: Cambridge University Press.

Ocasio, W., 1994. Political dynamics and the circulation of power: CEO succession in US industrial corporations, 1960-1990. *Administrative Science Quarterly*, pp.285-312.

Ong, P. L. 2009. Identity Matters: Ethnic Perceptions and Concerns. In: T. G. Lim, A. Gomes and A. Rahman. eds. *Multiethnic Malaysia: Past, Present and Future*Malaysia. SIRD and MiDAS@UCSI University, pp. 463-482.

Orlitzky, M. 2001. Does firm size confound the relationship between corporate social performance and firm financial performance? *Journal of Business Ethics* 33(2), pp. 167-180.

Pareto, V. 1968. *The Rise and Fall of the Elites*. Totowa, NJ: Bedminster Press

Park, Y.W. and Shin, H.H. 2004. Board composition and earnings management in Canada. *Journal of Corporate Finance* 10(3), pp. 431-457.

Parrino, R. et al. 2003. Voting with their feet: Institutional ownership changes around forced CEO turnover. *Journal of Financial Economics* 68(1), pp. 3-46.

Pearce, J.A. and Zahra, S.A. 1992. Board composition from a strategic contingency perspective. *Journal of Management Studies* 29(4), pp. 411-438.

Peasnell, K.V. et al. 2005. Board monitoring and earnings management: do outside directors influence abnormal accruals? *Journal of Business Finance & Accounting* 32(7-8), pp. 1311-1346.

Pelto, P.J. 1968. The differences between "tight" and "loose" societies. *Transaction*, 5(5), pp. 37-40.

Pepper, A. and Gore, J. 2015. Behavioral agency theory: New foundations for theorizing about executive compensation. *Journal of Management* 41(4), pp. 1045-1068.

Pfeffer, J. 1983. Organizational demography. In: Larry L., C. and Barry M. S. eds. *Research in organizational behavior*. 5th ed. Greenwich, CT: JAI Pres, pp. 299- 357.

Pfeffer, J. and Salancik, G. R. 1978. *The external control of organizations: a resource dependence perspective.* New York: Harper & Row.

Phinney, J.S. 1990. Ethnic identity in adolescents and adults: review of research. *Psychological Bulletin* 108(3), p. 499.

Quillian, L. and Campbell, M.E. 2003. Beyond black and white: The present and future of multiracial friendship segregation. *American Sociological Review* 68(4), pp. 540-566.

Qu, W. and Leung, P. 2006. Cultural impact on Chinese corporate disclosure–a corporate governance perspective. *Managerial Auditing Journal* 21(3), pp. 241-264

Ramasamy, B. et al. 2007. Corporate social performance and ethnicity: A comparison between Malay and Chinese chief executives in Malaysia. *International Journal of Cross-Cultural Management* 7(1), pp. 29-45.

Rangan, S. 1998. Earnings management and the performance of seasoned equity offerings. *Journal of Financial Economics* 50(1), pp. 101-122.

Rashid, M.Z.A. et al. 1997. Corporate Cultures and Work Values in Dominant Ethic Organizations in Malaysia. *Journal of Transnational Management Development* 2(4), pp. 60-72.

Rashid, M.Z.A. and Ho, J.A. 2003. Perceptions of business ethics in a multicultural community: The case of Malaysia. *Journal of Business Ethics* 43(1), pp. 75-87.

Roberts, M.R. and Whited, T.M. 2013. Endogeneity in empirical corporate finance. In: Constantinides, G., Harris, M., and Stulz, M. eds. *Handbook of the economics of finance*. 2nd ed. Oxford: Elsevier, pp. 493-572.

Rose, J.M. et al. 2014. Will disclosure of friendship ties between directors and CEOs yield perverse effects? *The Accounting Review* 89(4), pp. 1545-1563.

Rosenbaum, P.R. and Rubin, D.B. 1983. The central role of the propensity score in observational studies for causal effects. *Biometrika* 70(1), pp. 41-55.

Ross, S.A. 1973. The economic theory of agency: The principal's problem. *The American Economic Revie*w 63(2), pp. 134-139.

Roychowdhury, S. 2006. Earnings management through real activities manipulation. *Journal of Accounting and Economics* 42(3), pp. 335-370.

Ruigrok, W. et al. 2006. Board characteristics and involvement in strategic decision making: Evidence from Swiss companies. *Journal of Management Studies* 43(5), pp. 1201-1226.

Sarji, A. 1989. Equity in public service in Malaysia. In: Tummala, K. ed. *Equity in public employment across nations*. United States: University Press of America. pp. 147-152.

Schermerhorn, J.R. 1994. Intercultural management training: An interview with Asma Abdullah. *Journal of Management Development* 13(3), pp. 47-64

Schmidt, B. 2015. Costs and benefits of friendly boards during mergers and acquisitions. *Journal of Financial Economics* 117(2), pp. 424-447.

Schulze, W.S. et al. 2001. Agency relationships in family firms: Theory and evidence. *Organization Science* 12(2), pp. 99-116

Schwartz, S.H. 1999. Cultural value differences: some implications for work. *Applied Psychology* 48, pp. 23–47.

Securities Commission Malaysia 2018. *Corporate governance strategic priorities 2017-2020*. Available at: https://www.sc.com.my/api/documentms/download.ashx?id=7373ce94-78e9-456b-9b8fc7749f11c08c [Accessed: 2nd August 2019]

Sellers, R.M. et al. 1998. Racial ideology and racial centrality as predictors of African American college students' academic performance. *Journal of Black Psychology* 24(1), pp. 8-27.

Sendut, H. 1991. Managing in a multicultural society: The Malaysian experience. *Malaysian Management Review* 26(1), pp. 61-69.

Shamsul, A.B. 1996. Nations-of-intent in Malaysia. *Asian Forms of the Nation* 323, pp. 347.

Shao, L. et al. 2010. National culture and dividend policy. *Journal of International Business Studies* 41(8), pp. 1391-1414.

Shao, L. et al. 2013. National culture and corporate investment. *Journal of International Business Studies* 44(7), pp. 745-763.

Shen, W. and Cannella Jr, A.A. 2002. Revisiting the performance consequences of CEO succession: The impacts of successor type, postsuccession senior executive turnover, and departing CEO tenure. *Academy of Management Journal* 45(4), pp. 717-733.

Shen, W. and Cannella Jr, A.A., 2002. Power dynamics within top management and their impacts on CEO dismissal followed by inside succession. *Academy of Management Journal*, *45*(6), pp.1195-1206.

Shivakumar, L. 2000. Do firms mislead investors by overstating earnings before seasoned equity offerings? *Journal of Accounting and Economics* 29(3), pp. 339-371.

Shipman, J.E. et al. 2017. Propensity score matching in accounting research. *The Accounting Review* 92(1), pp. 213-244.

Shi, W. and Tang, Y. 2015. Cultural similarity as in-group favoritism: The impact of religious and ethnic similarities on alliance formation and announcement returns. *Journal of Corporate Finance* 34, pp. 32-46.

Shukeri, S.N. et al. 2012. Does board of director's characteristics affect firm performance? Evidence from Malaysian public listed companies. *International Business Research* 5(9), pp. 120.

Siegel, J.I. et al. 2011. Egalitarianism and international investment. *Journal of Financial Economics* 102(3), pp. 621-642.

Smith, K.K. 1983. Social comparison processes and dynamic conservatism in intergroup relations. *Research in Organizational Behavior* 5, pp. 199-233.

Smith, S. et al. 2014. Ethnic ingroup friendships in schools: Testing the by-product hypothesis in England, Germany, the Netherlands and Sweden. *Social Networks* 39, pp. 33-45.

Singh, H. 2001. Ethnic conflict in Malaysia revisited. *Commonwealth & Comparative Politics* 39, pp. 42-65.

Staerklé, C. et al. 2010. Ethnic minority-majority asymmetry in national attitudes around the world: A multilevel analysis. *Political Psychology* 31(4), pp. 491-519.

Staiger, D. and Stock, J.H. 1997. Instrumental variables regression with weak instruments. *Econometrica: Journal of the Econometric Society* 65(3), pp. 557-586.

Starbuck W.H. 1976. Organizations and their environments. In: Dunette MD. ed. *Handbook of industrial and organizational psychology*. Chicago, Il: Rand McNally, pp. 345–354.

Stein, L.C. and Zhao, H. 2019. Independent executive directors: How distraction affects their advisory and monitoring roles. *Journal of Corporate Finance* 56, pp. 199-223.

Stock J, and Yogo M. 2005. Testing for weak instruments in linear IV regression. In: Andrews, D. ed. *Identification and inference for econometric models*. New York, NY: Cambridge University Press.

Stockwell, A.J. 1982. The white man's burden and brown humanity: colonialism and ethnicity in British Malaya. *Asian Journal of Social Science* 10(1), pp. 44-68.

Storz, M.L. 1999. Malay and Chinese values underlying the Malaysian business culture. *International Journal of Intercultural Relations* 23(1), pp. 117-131.

Stulz, R.M. and Williamson, R. 2003. Culture, openness, and finance. *Journal of Financial Economics* 70(3), pp .313-349.

Suess-Reyes, J. 2017. Understanding the transgenerational orientation of family businesses: the role of family governance and business family identity. *Journal of Business Economics* 87(6), pp. 749-777.

Sunar, D.G. 1978. Stereotypes of the powerless: A social psychological analysis. *Psychological Reports* 43(2), pp. 511-528.

Sundaram, J.K. 1989. Malaysia's new economic policy and national unity. *Third World Quarterly* 11(4), pp. 36-53.

Tabellini, G. 2008. Institutions and culture. *Journal of the European Economic association* 6(2-3), pp. 255-294.

Tajfel, H. 1972. Social categorizationn. English manuscript of 'la categorisation sociale.' In: Moscovici. S. ed. *Introduction a la psychologie sociale*. 1st ed. Paris: Larousse, pp. 272-302

Tajfel, H. 1982. Instrumentality, identity and social comparisons. In: H. Tajfel Ed. Ed. *Social identity and intergroup relations.* Cambridge, England: Cambridge University Press, pp. 483-507.

Tajfel, H. and Turner, J. C. 1986. The social identity theory of intergroup behavior. In: Worchel, S. and Austin, G. Eds. *Psychology of intergroup relations.* 2nd ed. Chicago, Il: Nelson-Hall, pp. 7-24.

Tajfel, H. et al. 1979. An integrative theory of intergroup conflict. *Organizational Identity: A Reader* 56(65), pp. 9-16.

Tan, E.K. 2001. From sojourners to citizens: managing the ethnic Chinese minority in Indonesia and Malaysia. *Ethnic and Racial Studies* 24(6), pp. 949-978.

Tee, C.M. and Rassiah, P. 2020. Ethnic board diversity, earnings quality and institutional investors: evidence from Malaysian corporate boards. *Accounting & Finance* 60(4), pp. 4257-4290.

Teoh, S. et al. 1998a. Earnings management and the post-issue performance of seasoned equity offerings. *Journal of Financial Economics* 50, pp. 63–99

Teoh, S. et al. 1998b. Earnings management and the long-term market performance of initial public offerings. *The Journal of Finance* 53, pp. 1935–1974

Terjesen, S. and Sealy, R. 2016. Board gender quotas: Exploring ethical tensions from a multi-theoretical perspective. *Business Ethics Quarterly* 26(1), pp. 23-65.

Terpstra-Tong, J.L. et al. 2014. Convergence and divergence of individual-level values: A study of Malaysian managers. *Asian Journal of Social Psychology* 17(3), pp. 236-243.

Thornhill, S. and Amit, R. 2003. Learning about failure: Bankruptcy, firm age, and the resource-based view. *Organization Science* 14(5), pp .497-509.

Tosi, H.L. and Greckhamer, T. 2004. Culture and CEO compensation. *Organization Science* 15(6), pp. 657-670.

Tosi, H.L. et al. 2000. How much does performance matter? A meta-analysis of CEO pay studies. *Journal of Management* 26(2), pp. 301-339.

Triandis, H.C. et al. 1986. The measurement of the etic aspects of individualism and collectivism across cultures. *Australian Journal of Psychology* 38(3), pp. 257-267.

Triandis, H.C. 1989. The self and social behavior in differing cultural contexts. *Psychological Review* 96(3), pp. 506.

Turner, J. C. 1984. Social identification and psychological group formation. In: H. Tajifel. ed. *The social dimension: European developments in social psychology*. 2nd ed. Cambridge, England: Cambridge University Press, pp. 518-538.

Turner, J.C. et al. 1987. *Rediscovering the social group: A self-categorization theory*. Oxford, England: Blackwell.

Tzeng, O.C. and Jackson, J.W. 1994. Effects of contact, conflict, and social identity on interethnic group hostilities. *International Journal of Intercultural Relations* 18(2), pp. 259-276.

Vafeas, N. 1999. Board meeting frequency and firm performance. *Journal of Financial Economics* 53(1), pp. 113-142.

Vafeas, N. 2005. Audit committees, boards, and the quality of reported earnings. *Contemporary Accounting Research* 22(4), pp. 1093-1122.

Veltrop, D.B. et al. 2018. The relationship between tenure and outside director task involvement: A social identity perspective. *Journal of Management* 44(2), pp. 445-469.

Verkuyten, M. 2006. Multicultural recognition and ethnic minority rights: A social identity perspective. *European Review of Social Psychology* 17(1), pp. 148-184.

Verkuyten, M. 2013. *Identity and cultural diversity: What social psychology can teach us*. Oxon, UK: Routledge.

Verkuyten, M. and Khan, A. 2012. Interethnic relations in Malaysia: Group identifications, indispensability and inclusive nationhood. *Asian Journal of Social Psychology* 15(2), pp. 132-139.

Volonté, C. 2015. Culture and corporate governance: The influence of language and religion in Switzerland. *Management International Review* 55(1), pp. 77-118.

Warner, J.B. et al. 1988. Stock prices and top management changes. *Journal of Financial Economics* 20, pp. 461-492.

Webster, G. 2010. *Malaysia: Asia's cultural melting pot*, *CNN*, 26 Oct. Available at: http://edition.cnn.com/2010/WORLD/asiapcf/10/22/malaysia.country.profile/index.html (Accessed: 27 July 2019).

Weisbach, M.S. 1988. Outside directors and CEO turnover. *Journal of Financial Economics, 20*, pp.431-460.

Westphal, J.D., 1998. Board games: How CEOs adapt to increases in structural board independence from management. *Administrative Science Quarterly*, pp. 511-537.

Westphal, J.D. 1999. Collaboration in the boardroom: Behavioral and performance consequences of CEO-board social ties. *Academy of Management Journal* 42(1), pp. 7-24.

Westphal, J.D. and Khanna, P. 2003. Keeping directors in line: Social distancing as a control mechanism in the corporate elite. *Administrative science quarterly* 48(3), pp. 361-398.

Westphal, J.D. and Zajac, E.J. 1995. Who shall govern? CEO/board power, demographic similarity, and new director selection. *Administrative Science Quarterly* 40(1*)*, pp. 60-83.

Westphal, J.D. and Zajac, E.J. 2013. A behavioral theory of corporate governance: Explicating the mechanisms of socially situated and socially constituted agency. *Academy of Management Annal*s 7(1), pp. 607-661.

Whetten, D. et al. 2014. Organizational identity and family business. In: Meilin, L., Nordqvist, and Sharma, P. eds. *The SAGE handbook of family business*, London: Sage, pp. 480-497.

Williamson, O.E. 2000. The new institutional economics: taking stock, looking ahead. *Journal of Economic Literature* 38(3), pp. 595-613.

Wiseman, R.M. et al. 2012. Towards a social theory of agency. *Journal of Management Studies* 49(1), pp. 202-222.

Wiseman R.M. and Gomez-Mejia L.R. 1998 A behavioral agency model of managerial risk taking. *Academy of Management Review* 23(1), pp. 33-53.

World Values Survey Waves 5–6. 2005–2014. *World Values Survey Association*. Available at: https://www.worldvaluessurvey.org/wvs.jsp

Wu, T.Y. 1980. *Roots of Chinese culture*. Singapore: Federal Publications.

Xie, B. et al. 2003. Earnings management and corporate governance: the role of the board and the audit committee. *Journal of Corporate Finance* 9(3), pp. 295-316.

Xin, K.K. and Pearce, J.L. 1996. Guanxi: Connections as substitutes for formal institutional support. *Academy of Management Journal* 39(6), pp. 1641-1658.

Yatim, P. et al. 2006, Governance structures, ethnicity, and audit Fees of Malaysian listed firms, *Managerial Auditing Journal* 21(7), pp. 757-782.

Yermack, D. 1996. Higher market valuation of companies with a small board of directors. *Journal of Financial Economics* 40(2), pp. 185-211.

Yong, H. H. 2004. *5 men & 5 ideas: Building national identity*. Kuala Lumpur, Malaysia: Pelanduk Publications (M) Sdn Bhd.

You, J. and Du, G. 2012. Are political connections a blessing or a curse? Evidence from CEO turnover in China. *Corporate Governance: An International Review* 20(2), pp. 179-194.

Yzerbyt, V. and Demoulin, S. 2010. Intergroup relations. In: S. T. Fiske, D. T. Gilbert, and G. Lindzey. eds. *Handbook of social psychology*. Hoboken, NJ: John Wiley & Sons, pp. 1024–1083.
Available at: https://doi.org/10.1002/9780470561119.socpsy002028

Zahra, S.A. and Pearce, J.A. 1989. Boards of directors and corporate financial performance: A review and integrative model. *Journal of Management* 15(2), pp. 291-334.

Zang, A.Y. 2012. Evidence on the trade-off between real activities manipulation and accrual-based earnings management. *The Accounting Review* 87(2), pp. 675-703.

Zawawi, D. 2008. Cultural dimensions among Malaysian employees. *International Journal of Economics and Management* 2(2), pp. 409-426.

Zhang, L. et al. 2020. A tiger with wings: CEO–board surname ties and agency costs. *Journal of Business Research* 118, pp. 271-285.

Zhang, X. et al. 2013. Individualism-Collectivism, private benefits of controls, and earnings management: a cross-culture comparison. *Journal of Business Ethics* 114(4), pp. 655-664.

Zheng, X. et al. 2012. National culture and corporate debt maturity. *Journal of Banking & Finance* 36(2), pp. 468-488.

Zhu, D.H. and Chen, G. 2015. Narcissism, director selection, and risk-taking spending. *Strategic Management Journal* 36(13), pp. 2075-2098.

Zhu, J. et al. 2016. Board hierarchy, independent directors, and firm value: Evidence from China. *Journal of Corporate Finance* 41, pp. 262-279.