BOARD COMPOSITION AND FIRM INTERNATIONALIZATION: ARE EMERGING MARKET MULTINATIONAL ENTERPRISES UNIQUE?

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Abstract

The paper explores the impact of board composition on the degree of firm internationalization for emerging market multinational enterprises (EMNEs). Departing from previous studies focused on developed market multinational enterprises (DMNEs), in light of institutional voids in emerging economies, we hypothesize the relationship of board size, insider leadership, board independence, and board interlock with the level of internationalization of EMNEs. Using data from 5,104 publicly listed Indian firms from 2012 to 2020, we conducted a Tobit panel regression. The results show that board size and insider leadership are negatively correlated, while board interlock has a positive relationship, and board independence was insignificant with the level of internationalization. The findings of the study contribute to the EMNE literature by providing context-specific knowledge on board composition and internationalization. Furthermore, the results of this study contribute to the corporate governance literature regarding board dynamics in the context of emerging markets, which differ significantly from board dynamics in developed market companies.

Keywords: Board Size, Insider Directorship, Board Independence, Board Interlock, Internationalization, Emerging Market Multinational Enterprises

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1. INTRODUCTION

Internationalization acts as a tool for the long-term sustainability of any firm, whether from developed or emerging markets (Barroso et al., 2011). The increasing liberalization in emerging economies, which has reduced trade barriers between countries (Khanna et al., 2006), has encouraged emerging market multinational enterprises (EMNEs) to actively engage in internationalization (Gaur & Kumar, 2009). However, in sharp contrast to developed market multinational enterprises (DMNEs), EMNEs often operate in environments characterized by institutional voids, weak enforcement and regulation, concentrated ownership, and informal governance structures (Khanna & Palepu, 2005; Puffer et al., 2010). The lack of robust institutions affects internationalization as well as the strategic performance of the firm (Khanna & Rivkin, 2001). Moreover, the absence of formal institutional settings is often replaced by informal mechanisms in emerging markets (Puffer et al., 2010), which changes the business dynamics, thereby altering theories and findings from studies of firms in developed markets (Clark & Soulsby, 1999). For instance, the existing literature on DMNEs suggests that more independent directors on the board will lead to higher internationalization (Sanders & Carpenter, 1998; Tihanyi et al., 2003) but such assumptions may not hold true in the case of EMNEs, as insider influence, concentrated ownership, and network governance mechanisms often dominate the context. Therefore, these distinctive characteristics of emerging markets limit the direct application of theories developed in the DMNE context and necessitate context-specific research on the drivers of internationalization.

While there are several factors that influence the internationalization of multinational enterprises (MNEs), existing studies highlight the critical importance of the board of directors in influencing critical decisions regarding the internationalization of firms (Boeker & Goodstein, 1991; Grinyer & Mckiernan, 1990). Although there are several studies on the board composition and firm performance of MNEs, most of the literature focuses on DMNEs, often overlooking the specific characteristics of governance structures in emerging markets (Ararat et al., 2015; Al Mamun & Badir, 2013; Shikha, 2017; Tiwari & Kumar, 2020; Watkins et al., 2009; Lu et al., 2022). Therefore, there is a need for empirical research in this direction, which is largely uncovered or remains understudied. Given the prevalence of informal institutions, institutional voids, and relational and network governance (Puffer et al., 2010; Clark & Soulsby, 1999), it is important to examine the influence of board characteristics on the internationalization of EMNEs and whether they differ from the developed market context.

The existing literature examining the relationship between board characteristics and firm internationalization, primarily for DMNEs (Shu et al., 2015), provides limited insight into the function of board characteristics in the emerging market context marked by the lack of a robust infrastructure, the presence of corruption, uncertainty, and non-existent rules and regulations (Khanna & Palepu, 2010). This study aims to address this important gap by examining four major corporate governance constructs — board size, insider directorship, board independence, and board interlock — on the level of internationalization in emerging economies. Accordingly, this study seeks to answer the following research question:

RQ: What is the impact of board characteristics, in particular board size, insider directorship, board independence, and board interlock, on the level of internationalization of EMNEs?

Using Tobit regression, a study was conducted on 5,104 Indian multinational firms listed on the National Stock Exchange of India (NSE) between 2012 and 2020. The results of the study support the hypotheses that board size and board connectivity have a negative and positive impact on firm internationalization, respectively. However, insider directorship has a negative impact on EMNE internationalization, and the impact of board independence is insignificant.

This study contributes to international business theory in general and contributes to the existing literature on EMNEs, in particular, by contextualizing and explaining the impact of emerging market characteristics on board dynamics in EMNE internationalization. This study further indicates that, unlike DMNEs, EMNEs are subject to greater market uncertainty and stakeholder dynamics and depend on informal governance mechanisms that influence how board characteristics influence strategic decisions to internationalize. Furthermore, this study also complements the corporate governance literature by describing the differential impact of board characteristics such as board size, independence, interlock, and insider directorship in an emerging market context.

The rest of the paper is structured as follows. Section 2 discusses the extant literature and hypotheses for this study. Section 3 describes the data and methodology used in the study. Section 4 tests the hypotheses using data of the Indian firms extracted from the Prowess database and presents the results. Section 5 analyzes the results. Finally, Section 6 concludes the paper.

2. LITERATURE REVIEW AND HYPOTHESES DEVELOPMENT

The board of directors consists of two major categories of directors — executive and non-executive directors (NEDs). Executive directors are the executive managers of the company (employees) who also serve as members of the board of directors of the organization. In the United States (U.S.), they are also called "inside directors" because they attain this position through internal promotions within the organizations. In contrast, the NEDs of the board are external to the firm and in the U.S. they are also called "outside directors". These individuals are appointed to the board for their expertise, networks, or previous experience in the line of work that the focal organization is engaged in (Kakabadse et al., 2001). There are two further categorizations of NEDs: 1) independent NEDs, and 2) non-independent NEDs. Independent NEDs have no relationship with the company in question other than simply being a director, so that they can exercise independent and impartial judgment in any decisions that the board will make. Again, directors often sit on the boards of other firms to strengthen the link between the firms (Booth & Deli, 1996) — a term is popularly known as "board interlock". All taken together, since the roles of each director in the decision-making policies differ, the impact of the board composition on firms' strategic policies and international performance is an interesting domain of research.

Previous studies have extensively examined the relationship between board characteristics and internationalization in the case of DMNEs (Sanders & Carpenter, 1998; Tihanyi et al., 2003), but there remains a critical gap in understanding whether these relationships and theories hold true in the context of EMNEs, especially due to the characteristics of the emerging market context such as institutional voids, informal and relational governance mechanism, and contextual uncertainty (Clark & Soulsby, 1999; Khanna & Palepu, 2005; Lu et al., 2022; Puffer et al., 2010). These differential institutional and organizational dynamics in the context of emerging markets such as India may result in different roles and influences of board characteristics compared to their counterparts in developed markets. This study seeks to address this significant gap by examining the influence of board characteristics such as size, independence, interlock, and insider directorship on the level of internationalization of EMNEs. The following subsections describe the relationships between each of these constructs and the internationalization of EMNEs and advance the research hypotheses.

2.1. Board size and internationalization

The board size has always been a critical determinant of the degree of internationalization of firms. Scholars have found that a larger board of directors favors the internationalization of firms for DMNEs (Kiel & Nicholson, 2003) because it captures more experience and resources that can help in the sustainability of the organization (Pfeffer, 1972, 1973; Sanders & Carpenter, 1998). The multiple perspectives and experiences obtained positively impact the outcome of corporate strategic decisions made by the top management team (Pearce & Zahra, 1992). From the perspective of Jensen and Meckling's (1976) agency theory, a larger board size strengthens the governance mechanism of the firm by reducing the dominant power of the chief executive officer (CEO) over any critical decision of the enterprise (Singh & Harianto, 1989). It was also found that the level of internationalization had a positive effect on the level of problem-solving by a large and diverse group (Hill, 1982; Jackson, 1992) due to better information processing ability (Dutton & Duncan, 1987) which facilitated the decision-making process (Haleblian & Finkelstein, 1993).

However, increasing board size has also been found to have a negative impact on many strategic changes initiated in uncertain environments (Goodstein et al., 1994). With more directors on the board, it becomes difficult for the top management team to reach a consensus on any major strategic decision of the firm that is time-constrained, which slows down the decision-making process in the organization (Harrison, 1987; Herman, 1981). This can be expected to be more prominent in the context of emerging markets, as these market environments are uncertain due to institutional voids (Khanna & Palepu, 2005). Furthermore, these markets operate on informal mechanisms consisting of relational proximity and intimacy instead of formal institutional rules and regulations (Mair et al., 2012). Now, as the number of board decision-makers increases, groups become less cohesive (Shaw, 1981), and the dynamics of larger groups make decision-making more difficult (Eisenhardt, 1989; Olson, 1982; Wiersema & Bantel, 1992). As intra-group conflicts increase, coordination becomes a vital issue for top management (Reilly et al., 1989), which in turn decreases the motivation of each member to contribute productively to the decision-making process. All this leads to firms with larger boards making fewer strategic decisions than firms with smaller boards (Judge & Zeithaml, 1992). Impaired decision-making becomes more pronounced in the presence of any environmental uncertainty (Meyer, 1982) — a major concern for EMNEs operating in institutional voids. Therefore, we hypothesize that as board size increases, the degree of internationalization, which is a difficult and critical decision for EMNEs, will decrease.

H1: Board size is negatively related to the degree of internationalization in emerging market economies.

2.2. Insider directorship and internationalization

Inside directors or executive directors are those who are the employees of the organizations and are promoted to the board of directors. Since they have information about the current projects of the firm, their input and ideas at board meetings have a significant impact on the decisions made by the team (Baysinger & Hoskisson, 1990; Judge & Zeithaml, 1992). They are more involved in the decision-making process of the firm (Johnson et al., 1993; Ruigrok et al., 2006), given that they are well aware of the strengths and weaknesses of the firm (Donaldson & Davis, 1991). Therefore, they are more sensitive to any internationalization opportunity of the firm and can make an informed decision after conducting relevant analysis. Since inside directors' compensation and career advancement are closely related to firm performance, they are more attentive to any external opportunities that can help the firm grow faster (Singh & Delios, 2017) and hence can be expected to positively impact the degree of internationalization of EMNEs. Therefore, we hypothesize:

H2: The number of executive directors is positively associated with the degree of internationalization of firms in emerging market economies.

2.3. Board independence and internationalization

The board of directors of any firm ideally performs three critical roles, which include: 1) resource provisioning, 2) collaboration, and 3) control over the factors that can create agency problems in the organization (Johnson et al., 1996). Since independent directors are more exposed to the external environment, their expertise can be one of the significant sources of competitive advantage for a firm, especially in the context of emerging markets (Gaur & Kumar, 2009; Al Mamun & Badir, 2013; Rhoades et al., 2001). Independent directors often serve on the boards of other firms. This helps the focal firm gain greater access to information, and hence it can benefit from its internationalization strategies (Sherman et al., 1998). Furthermore, it is important to note that independent directors also help EMNEs overcome the "liability of foreignness" problem (Luo, 2007). They can also provide critical insights and resources to firms choosing to enter a foreign market (Baysinger & Hoskisson, 1990; Chen et al., 2016). Such a resource-provisioning role of the directors in the firm, owing to their increased access to information and heavier networking abilities (Carpenter & Westphal, 2001; Goodstein et al., 1994; Hillman et al., 2000; Kakabadse et al., 2001), can be expected to positively impact the international performance of EMNEs. EMNEs need to build strong network ties (Boyd, 1990), overcome resource procurement challenges (Chacar & Vissa, 2005; Elango & Pattnaik, 2007; Khanna & Palepu, 2000), and gain legitimacy (Bazerman & Schoorman, 1983) in foreign markets. Hence, we hypothesize:

H3: The number of independent directors is positively related to the degree of internationalization of firms in emerging market economies.

2.4. Board interlocking and internationalization

Board interlocking is an interesting aspect of corporate governance that has been explored in the existing literature. Few indicated it to be a "double-edged sword" (Jackling & Johl, 2009) since multiple directorships affect directors' commitment to a single board (Core et al., 1999; Shivdasani & Yermack, 1999) and have the potential for increased opportunism (Fich, 2005; Rosenstein & Wyatt, 1994). However, for EMNEs, the role of directors' resource provision through interlocking is an important factor (Saeed et al., 2017; Westphal, 1999). These firms purchase capital resources from the market using director networks (Mizruchi & Stearns, 1994). They can also provide the knowledge needed to make any critical strategic decision by the firm's top management (Judge & Zeithaml, 1992; Palmer et al., 1993). Directors of one firm gain strategic knowledge about another firm (Fahlenbrach et al., 2010; Perry & Peyer, 2005), by means of board interlock. Strengthening network ties between firms, in turn, reduces information uncertainty about any resource on which both firms depend (Pettigrew, 1992) and the time to gain and process such information (Dearborn & Simon, 1958; Kor & Sundaramurthy, 2009).

The requirement for such skills is more pronounced for EMNEs when these firms decide to enter international markets (Sukumara Panicker & Upadhyayula, 2020). EMNEs generally have fewer resources than the multinationals of developed countries (Aulakh et al., 2000). Thus, directors' network ties can be beneficial for these firms in the sense that they help firms gain the necessary information and adaptability in stages of environmental uncertainty (Barroso et al., 2011; Hitt et al., 2006). It also provides EMNEs with resources in the form of new business partners, suppliers, and customers (Booth & Deli, 1996; Pfeffer, 1972). It also prepares firms to deal with cultural and market-related compatibility issues that they may face in the international market (Caves, 1971; Kostova & Zaheer, 1999). Therefore, board interlocks are found to work in favor of reducing resource constraints of EMNEs (Mizruchi, 1996) for successful internationalization. Hence, we hypothesize:

H4: Increasing board interlock has a positive relationship with the degree of internationalization of firms in emerging economies.

3. RESEARCH METHODOLOGY

3.1. Sample selection

We test our hypotheses using data from the Prowess database published by the Centre for Monitoring Indian Economy (CMIE). We select all firms that are listed in the NSE. Our sample includes data for Indian firms for the period 2012–2019. We chose this period specifically to avoid any residual effects of the financial crisis as well as the COVID-19 pandemic on the results of this study. The initial dataset included 5202 firms, and after removing missing values, the final dataset contains 5103 unique firms and 11129 firm-year data points. We use India as a proxy for an emerging economy (Chakrabarti et al., 2008; Jain, 2006) to observe the differential impact of corporate governance of these firms on the degree of internationalization of EMNEs as opposed to firms operating in developed countries. The final dataset contains firms from all sectors, including financial, non-financial, and even state-owned enterprises.

3.2. Dependent variable

We measured the degree of internationalization using the logarithm of foreign assets owned by a firm. This is in line with previous studies of firms in emerging markets (Singh & Delios, 2017; Singh & Gaur, 2013).

3.3. Independent variables

Our explanatory variables included board size, board independence, insider directorship, and board interlock. All these variables had been extracted from the report on director types from the Prowess database. Board size is calculated by counting each member on the board in each year of every company. Board independence is measured using the number of independent directors by the total board size. Similarly, insider directorship is measured by dividing the number of executive directors in the firm by the total board size. Board interlock is measured by dividing the number of directors interlocked by the total number of directors.

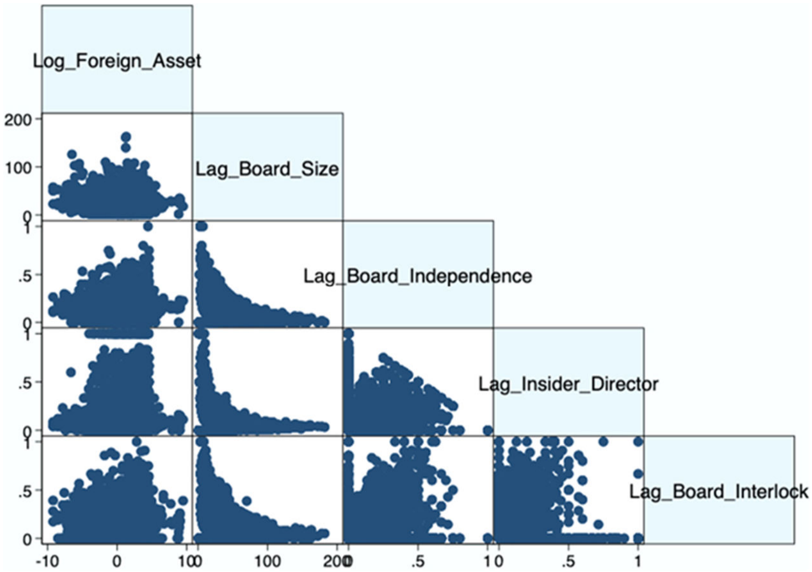
3.4. Control variables

We controlled for firm size, foreign ownership, firm age, past performance, and business group (BG) affiliation of firms. Firm size is measured using the logarithm of the firm's total assets. Foreign ownership is the sum of investments made in the firm by foreign promoters and foreign institutional investors. Firm age is the difference between the observation year and the year of incorporation of the firm. Past performance is captured using the lagged return on assets (ROA). Firms affiliated with BGs were coded as 1, while others were coded as 0 (Aguilera et al., 2024). Finally, the first two digits of the National Industry Classification (NIC) were used as a dummy variable along with a year dummy variable.

3.5. Methodology

We tested our hypotheses using a panel Tobit model in Stata 17 software. We used the Tobit model because our dependent variable (*Log_Foreign Assets*) is censored towards zero. The graphical representation of the same can be seen in Figure 1. This makes sense because many firms do not invest in foreign assets every year, and therefore the data points are clustered towards zero. In performing the analysis, we regressed the lag values of the explanatory variables on the dependent variable because this gives a better picture of the causal relationship.

Figure 1. Censoring of data



Source: Authors' elaboration.

4. RESEARCH RESULTS

Table 1 (see Appendix) illustrates the results of this study. Model 1 tested all controls for the degree of internationalization of firms in an emerging market economy, such as foreign ownership, firm age, firm size, ROA, and BG affiliation. Most of these controls were significantly related to the degree of internationalization, indicating the importance of these controls. Model 2 tested the first hypothesis (*H1*), which was supported. This result provides insight into the dynamics of an emerging market economy and why it is important for scholars to study the same phenomenon in different contexts.

Model 3 found that the number of executive directors was negatively related to the degree of internationalization of firms in an emerging market economy (the relationship was significant), which is contrary to the hypothesized relationship (*H2*). Model 4 tested the relationship between the number of independent directors and the degree of internationalization of firms in an emerging market economy. However, the relationship was found to be insignificant (*H3*: Not supported). We hypothesize that this may be due to the fact that independent directors do not have compensation tied to firm performance, and therefore their impact on international performance is not pronounced for EMNEs, consistent with an agency theory perspective. Model 5 tested the relationship between the increase in board interlock and the degree of internationalization of firms in an emerging economy. As hypothesized, the relationship was found to be positive and significant (*H4*: Supported). This means that the board interlock or the presence of directors on the board of two or more companies would contribute to increased levels of internationalization, possibly owing to the potential of interlocking directors to create meaningful connections between firms.

5. DISCUSSION OF THE RESULTS

The impact of board composition on international performance has interesting outcomes for EMNEs, as indicated by the outcomes of this study. We find support for two of the four hypotheses. Board size is negatively related to the degree of internationalization of the EMNEs. This indicates the prevalence of informal mechanisms in emerging markets, which is worsened by larger board sizes. The different result of this study from those conducted in developed market settings highlights the context specificity required to study EMNEs' internationalization cases (Clark & Soulsby, 1999). Since EMNEs operate in uncertain external environments, diversity of opinions may reduce group cohesion, thereby influencing critical strategic decisions (e.g., internationalization) of firms.

Second, our results show that insider leadership has a negative impact on the degree of internationalization for EMNEs. Although this is contrary to our hypotheses, the result is interesting. Insider leadership brings important expertise and value to the board. However, there is a possibility that since they directly report to the CEO/chairman, this affects their decision-making freedom in board meetings. In addition, insider directors are often criticized for being more focused on the short-term financial goals of firms rather than making critical strategic decisions (Pearse et al., 2022), which may be a plausible explanation for the negative result of *H2*.

Third, the insignificant relationship of independent directors with the level of firm internationalization is also an interesting result. The reason for this finding may be that independent directors do not receive compensation from the company, so they do not have enough incentive to participate in the firm's critical decisions (Jackling & Johl, 2009; Ntim, 2011). For this reason, their main focus is on the factors related to firm compliance (Zahra & Pearce, 1989). Moreover, they are often appointed by firms for symbolic purposes to enhance legitimacy rather than to make critical strategic decisions for the organization (Westphal & Zajac, 1998).

Finally, the positive effect of board interlock on the level of internationalization is convincing. Given the role of directors in providing resources in emerging markets (Saeed et al., 2017; Westphal, 1999), one might expect that since they sit on the boards of several firms, they will be able to attract more resources in terms of expertise, networks, information, etc. (Carpenter & Westphal, 2001; Goodstein et al., 1994; Hillman et al., 2000; Kakabadse et al., 2001). This is more pronounced for emerging market MNEs, as interconnected directorates often enhance firms' credibility in international markets (Watkins-Fassler et al., 2024). Furthermore, interlocking directorship also facilitates EMNEs' access to new foreign markets and technologies, which eventually has a positive impact on their international performance (Aalbers & Ma, 2023).

Our study contributes to the literature on international business as well as the corporate governance of emerging markets. Since most studies on the impact of board structure on international business have been conducted in the context of developed markets, the results of this study can inform the literature on the importance of institutional context when studying such a phenomenon. Thus, this study points to the relevance of context specificity for the study of international business. We also contribute to the literature on corporate governance. Previous studies have mostly cited the agency problem to examine the role of board structure on firm performance. Although the agency problem is important, it is the scarcity of resources in the weak institutional context of emerging markets that provides rich insights for research in these markets. Therefore, the corporate governance literature should embrace such context-rich insights to enrich the existing knowledge base. In addition, we encourage future research to examine the joint effects of these constructs to develop a better understanding of the board structure in emerging markets and their impact on firm performance. Furthermore, future studies with data from multiple emerging economies on board processes (Wan & Ong, 2005) would also provide valuable insights and be able to establish generalizability in such contexts.

6. CONCLUSION

Corporate governance research has been largely conducted in developed markets. However, the growing number of EMNEs and their unique market conditions have attracted the interest of scholars from different countries. The strategic choices of these firms differ significantly from those of DMNEs, and it has been important to conduct more research on EMNEs to understand the contextual specifics of these organizations.

In this paper, we reviewed the literature on four key corporate governance constructs — board size, insider directorship, board independence, and board interlock — in the context of the internationalization of EMNEs. We empirically tested and found support for two of our four hypotheses. The main contribution of the study is the confirmed findings that board size and insider directorship have a negative impact on the degree of internationalization of EMNEs, highlighting the unique business dynamics in the emerging market context.

This paper is not without limitations. First, we had to remove a lot of firm records due to missing values. Second, the data are from 2012–2019, which could be extended to obtain more robust results. Furthermore, an interesting area of future studies could be to test the joint effects of these constructs on the level of internationalization of EMNEs with data from multiple countries. This will have critical theoretical implications as it will contribute to the growth of the literature on EMNEs but will also have critical managerial implications for the top management team that operates in such markets under severe resource constraints.

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APPENDIX

Table 1. Results of the Tobit models

Variables	*Model 1 Controls only model*			*Model 2 H1: Board size*			*Model 3 H3: Independent directorship*			*Model 4 H2: Insider directorship*			*Model 5 H4: Board interlock*		
	B-value	*Std. dev.*	*p-value*	*B-value*	*Std. dev.*	*p-value*	*B-value*	*Std. dev.*	*p-value*	*B-value*	*Std. dev.*	*p-value*	*B-value*	*Std. dev.*	*p-value*
Board_Size				-0.003	0.001	0.008									
Board_Independence							0.051	0.118	0.665						
Insider_Directorship										-0.117	0.078	0.032			
Board_Interlock													0.206	0.09	0.022
Firm_Size	-0.072	0.013	0.00	-0.066	0.015	-0.096	-0.079	0.014	0	-0.08	0.014	0	-0.081	0.014	0
Foreign_Ownership	0	0	0.48	0	0	0	0	0	0.513	0	0	0.5	0	0	0.544
Firm_Age	-0.001	0.002	0.522	-0.002	0.002	-0.006	-0.002	0.002	0.268	-0.002	0.002	0.255	-0.003	0.002	0.218
Past_Performance	0	0	0.731	0	0	0	0	0	0.853	0	0	0.817	0	0	0.863
BG_Affiliation	0.204	0.081	0.011	0.203	0.083	0.041	0.206	0.083	0.012	0.204	0.083	0.013	0.199	0.083	0.016
Industry dummy	-0.005	0.002	0.01	-0.005	0.002	-0.009	-0.005	0.002	0.008	-0.006	0.002	0.007	-0.005	0.002	0.008
N	11129			11129			11129			11129			11129		
p-value	0.000			0.000			0.000			0.000			0.000		

Source: Authors' elaboration.