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**CORPORATE BOARD, DIVERSIFICATION
STRATEGIES, AND THE VALUE OF DIVERSIFIED
LISTED COMPANIES: THE MODERATING EFFECT
OF MANAGERS' WEALTH MAXIMIZATION ON
DIVERSIFICATION VALUE**

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**DOCTOR OF PHILOSOPHY
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**CORPORATE BOARD, DIVERSIFICATION STRATEGIES, AND THE
VALUE OF DIVERSIFIED LISTED COMPANIES: THE MODERATING
EFFECT OF MANAGERS' WEALTH MAXIMIZATION ON
DIVERSIFICATION VALUE**

BY



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In Fulfillment of the Requirement for the Degree of Doctor of Philosophy**



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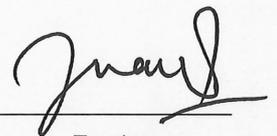
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ABSTRACT

Keeping in view the important role of Malaysian corporate sector in the country's growth and development, and proliferation of diversified companies, this study was conducted on Public Listed Companies (PLCs) on Bursa Malaysia's Main Market. This study examines the relationship between corporate board, diversification, the value of diversified listed companies in Malaysia, with the moderating effect of managers' wealth maximization on diversification strategies and value. Secondary data was obtained mainly from the companies' annual reports published. This study utilised sample of 490 PLCs, and employed multiple regression techniques to analyse data and draw conclusions. Findings of the study reveals that board independence and risk management committee have positive impact on diversification value. Meanwhile board size, audit independence, audit committee size and tenure of independent directors have negative impact on the diversification value. Furthermore, the findings show that related diversification strategy positively affects diversification value, whereas unrelated diversification strategy has a negative impact on diversification value. Managers' wealth maximization positively moderates the relationship between related diversification strategy and diversification value. However, managers' wealth maximization shows a negative moderation relationship between unrelated diversification strategy and diversification value. Related diversifiers seem to outperform unrelated diversifiers on all the three diversification value dimensions (sales, ebit & asset). The findings supports the agency and resource dependency theories on the view that enhanced corporate governance practices could contribute towards increasing diversification value. In addition, the findings may also assist corporate managers to get rid of the dilemma on their choice of the best and most profitable diversification strategies. Generally, this study provides additional insights to policy makers and regulators towards improving corporate governance policies in the future. It may also help to increase understanding the relationship between corporate governance practices, diversification strategies and firm value.

Key words: corporate governance, diversification strategies, diversification value, managers' wealth maximization, public listed companies, Malaysia.

ABSTRAK

Mengambil kira peranan penting sektor korporat Malaysia dalam pertumbuhan dan pembangunan negara dan percambahan syarikat yang pelbagai, kajian ini dijalankan ke atas Syarikat Tersenarai Awam (PLC) di Pasaran Utama Bursa Malaysia. Kajian ini mengkaji hubungan antara lembaga korporat, kepelbagaian, nilai syarikat tersenarai yang berlainan Malaysia, dan kesan penyederhanaan pemanfaatan kekayaan pengurus terhadap strategi kepelbagaian. Data sekunder diperolehi daripada laporan tahunan syarikat. Kajian ini menggunakan sampel 490 PLC, dan menggunakan teknik regresi berganda untuk menganalisis data dan membuat kesimpulan. Dapatan kajian menunjukkan bahawa kebebasan lembaga, jawatankuasa pengurusan risiko mempunyai kesan positif ke atas nilai kepelbagaian. Manakala saiz lembaga, kebebasan audit, saiz jawatankuasa audit dan tempoh pengarah bebas mempunyai kesan negatif terhadap nilai kepelbagaian. Dapatan kajian juga bahawa strategi kepelbagaian yang berkaitan memberi kesan positif kepada nilai kepelbagaian, sedangkan strategi kepelbagaian yang tidak berkaitan mempunyai kesan negatif terhadap nilai kepelbagaian. Pengoptimuman kekayaan pengurus secara positif menyederhana hubungan antara strategi kepelbagaian yang berkaitan dengan nilai kepelbagaian. Walau bagaimanapun, pengoptimuman kekayaan pengurus mempunyai hubungan penyederhanaan negatif antara strategi kepelbagaian yang tidak berkaitan dan nilai kepelbagaian. Pempelbagaian yang berkaitan seolah-olah mengatasi pemelbagaian yang tidak berkaitan pada semua tiga dimensi nilai kepelbagaian (jualan, ebit & aset). Penemuan ini menyokong teori agensi dan teori ketergantungan sumber berkenaan pandangan bahawa amalan tadbir urus korporat yang lebih baik boleh menyumbang ke arah meningkatkan nilai kepelbagaian. Di samping itu, penemuan ini juga boleh membantu pengurus korporat untuk menyingkirkan dilemma ke atas pilihan strategi pelbagaian yang terbaik dan paling menguntungkan. Secara amnya, kajian ini memberikan pandangan tambahan kepada pembuat dasar dan pengawal selia untuk meningkatkan dasar tadbir urus korporat pada masa akan datang. Ia juga boleh membantu meningkatkan pemahaman hubungan antara amalan tadbir urus korporat, strategi kepelbagaian dan nilai firma.

Kata kunci: tadbir urus korporat, strategi kepelbagaian, nilai kepelbagaian, pemaksimuman kekayaan pengurus, syarikat tersenarai awam, Malaysia.

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LIST OF ABBREVIATIONS

ACE	Access Certainty Efficiency
AGMs	Annual General Meetings
APEC	Asia-Pacific Economic Co-operation
APO	Asian Productivity Organization
BCG	Boston Consulting Group
BNM	Bank Negara Malaysia
BRC	Blue Ribbon Committee
CEO	Chief Executive Officer
CMA	Capital Market Authority
CMDF	Capital Market Development Fund
CMP	Capital Market Masterplan
COSO	Committee of Sponsoring Organizations of the Treadway Commission
ERM	Enterprise Risk Management
EU	European Union
FCCG	Financing Committee on Corporate Governance
FRC	Financial Reporting Commission
FTSE	Financial Times Stock Exchange
GCC	Gulf Co-operation Council
GDP	Gross Domestic Product
GTP	Government Transformation Program
IAF	International Audit Function
IASB	International Accounting Standard Board
IMF	International Monetary Fund
IR	Incentive Ratio
MASB	Malaysia Accounting Standard Board

MCCG	Malaysian Code on Corporate Governance
MFRS	Malaysia Financial Reporting Standard
MIA	Malaysian Institute of Accountants
MICG	Malaysia Institute of Corporate Governance
MICPA	Malaysian Association of Certified Public Accountants
MIDA	Malaysian Investment Development Authority
MSWG	Minority Shareholders Watchdog Group
NEAC	National Economic Advisory Council
OECD	Organization for Economic Co-operation and Development
PCAOB	Public Company Accounting Oversight Board
PLC	Public Listed Company
RMC	Risk Management Committee
SC	Securities Commission
SIC	Standard Industrial Classification
SOX	Sarbane-Oxley Act
UK	United Kingdom
USA	United States of America
USSR	Union of Soviet Socialist Republic

CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

For the past few decades, the issue of corporate governance has dominated much of intellectual debates. The discussions has gained considerable responsiveness due to the trend of governance failure in some firms in both developed and developing markets, like United States, Germany, United Kingdom, India, Malaysia, Indonesia and other parts of the world which has called for the efficacy of the existing corporate governance structures to protect the interest of shareholders (Maigoshi, 2017). Many reforms (i.e. on corporate structures) have been made to ensure that boards of directors are effective in discharging their role. Generally, the codes of good governance in various countries, call for more independent directors on the boards (Germain, Galy, & Lee, 2014). In Malaysia, the Malaysian Code on Corporate Governance (MCCG) that was first introduced in March 2000 which was later incorporated into Bursa Malaysia's listing rules in 2001. The code sets out the basic principles and best practices of good governance as well as describes optimal corporate governance mechanisms and internal procedures.

The issuance of the MCCG, was parallel with the establishment of corporate governance guidelines in several other countries, such as the United States (Sarbanes-Oxley Act), United Kingdom (Cadbury & Hampel Report), and the Australian (Bosch Report). These corporate governance codes were aimed at setting out principles and best practices for firms to use in their operations in order to attain an optimal governance structure. The codes provides guidelines comprises of matters such as size and composition of the board,

establishment of board committees, audit committees, board diversity and procedures for the appointment of new directors and the duration of their tenure. As a whole, the code provides guidelines for the board in implementing their roles, which involves monitoring role in order to ensure increase in shareholders' wealth and firm value (Kassim, 2013). The board of directors is seen as one of the most prominent corporate governance mechanisms since they are expected to protect and monitor the interest of shareholders as well as firm performance (Kassim, Ishak, & Manaf, 2013).

The core mechanisms of corporate governance are specially designed to overcome the severity of agency problems in modern corporations (Salina & Nazrul, 2017; Arnoldi & Muratova, 2019). Meanwhile, Jensen and Meckling (1976) suggest that agency problems ascend due to the separation of ownership and control which results in a potential clash of interest between owners and managers. Managers who quest for self-interests are doubtful to maximize returns to shareholders as they have a tendency to misuse corporate assets, through involvement in high risk or imprudent investment to the detriment of capital providers (John & Senbet, 1998; Salina & Nazrul, 2017). Though the conflict of interest may decrease firm's value and interfere with corporate investment strategy (O'Connor & Rafferty, 2012). In accordance, a good corporate structures and procedures are indispensable in order to protect the shareholders' interest and reduce the possibility of loss in firm value due to the separation of ownership and control.

Following the Asian financial crisis, the development of corporate governance in Malaysia has been significant, in order to restore market confidence that was smashed due to the crisis (Anum, 2010; Zabri, Ahmad, & Wah, 2016). The study of Salina and Nazrul (2015)

revealed that poor corporate governance is the major contributing factor that leads to the economic turmoil in 1997. The weak control over corporate governance includes less activities of reforming company structure, over-leveraging debts, lack of disclosures on transparency and accountability, and poor credit control systems (Alnasser, 2012). Moreover, the high leveraging of corporations turns out to be more severe in the period of the crisis, which is one of the leading factors in the Asian financial disaster (Driffield, Mahambare & Pal, 2007). The crisis severely affected Malaysia, as well as other countries in the region, including Indonesia, Thailand and South Korea (Kassim, 2013).

Based on the Malaysian experience, lots of corporations were at the mercy of debt financing with banking institutions prior to the crisis (Suto, 2003). As the crisis hit, risk aversion of banks heightened which leads to corporations' travail from liquidity chomp and were unable to roll over their loans from banks (Kassim, 2013). Consequently, the condition of corporations further worsened as a result of corporate failure ascribed to poor corporate governance. Meanwhile, one of the befitting strategy put in place by the Malaysian Financing Committee on Corporate Governance (FCCG) in dealing with corporate failure during the period of the Asian financial crisis was perhaps the establishment of the MCCG. Since the major aims of the code is to set out principles and guidelines that will eventually lead to increase in shareholders' wealth and firm value, hence the investigation on the effect of corporate board on firm value of diversified public listed firms is needed in Malaysia. Based on the contribution of the public listed companies to the Malaysian economy and given the importance of good business judgment.

Common theories employed in prior studies on corporate governance such as the agency, resource dependency and stakeholders theory, is explained based on the jurisdictions where corporate issues (for instance, maximization of shareholders' wealth and increase in firm value) are being examined (Marie, 2014). Corporate governance highlights a set of relationships between the controlling managers, its board, shareholders and other stakeholders. It offers the structures through which the goals of the company are set and measures for achieving those objectives and monitoring performance are determined (OECD, 2004). The research work of Ishak (2004), also view corporate governance as a set of rules, laws, policies instruments and measures which affects the operations of the company. In addition, corporate governance has been viewed as “the process and structures used to direct and manage the business and affairs of the company towards enhancing business prosperity and corporate accountability with the ultimate objective” (FCCG). Zabri et al. (2016) further argued that from the economic perspective, corporate governance plays a crucial role in achieving an efficiency in which scare resources are directed towards investment strategy with the highest returns.

A sound corporate governance mechanism should provide incentives for the board and controlling managers to ensure they achieve the objectives and interest of the corporation. However, the shareholders should influence the creation of the corporate mechanism for proper monitoring and assessment of controlling managers in their duties to the company. The existence of an effective corporate governance within a company and across an economy as a whole may assist in providing a degree of confidence necessary to attract more investment and enhance the operation of the market economy (OECD, 2004). In addition, corporate governance mechanisms are essential in aligning the interest of

managers to shareholders and protect stakeholders' interest (Becht & Böhmer, 2003; Latif, 2018). Furthermore, Walker and Fox (2002) and Ishak and Napier (2006) argued that corporate governance is one of the ways to legally protect the interest of shareholders from been expropriated by managers and controlling owners.

On the other hand, to diversify or to remain focused is one of the most essential requests for a company's strategist (Marinelli, 2011). In the West, the tendency of diversifying into different industries started in 1960's which continued till 1970's, nonetheless many companies started to refocus and restructure themselves during 1980's (David, O'Brien, & Yoshikawa, 2010; Doaei, Davarpanah & Sabzi, 2017). Corporate diversification can be partitioned into different categories. For instance, there is a national or international (global) diversification (Mehmood & Hilman, 2017), as well as diversification within the same industry (related) or in an entirely different industry (unrelated) (Erdorf et al., 2013). Meanwhile, corporate diversification strategies may have diverse impact on firm value.

Theories such as market power view (Palich, Cardinal, & Miller, 2000; Mehmood, 2015), resource based view (Wernerfelt, 1984; Bryant & Davis, 2012), internal capital market efficiency (Berger & Ofek, 1995), transaction cost economics theory (Williamson, 1998), and agency theory (Jensen, 1986), provide rationales for increased diversification among the companies. Research conducted in context of Asian economies also reported high levels of product diversification in those economies (Lins & Servaes, 2002). Transaction cost economics and internal capital market efficiency, in particular, provide reasons for high diversification of companies in many Asian economies. Empirical studies by Chakrabarti,

Singh, and Mahmood (2007) and Mishra and Akbar (2007) conducted in developing countries provide support for the transaction cost and internal capital market efficiency.

For the past decade, divergence record of some companies also indicates increased diversification on the part of Malaysian organizations (Ahmad, Ishak & Manaf 2003; Doaei, Anuar, & Ismail, 2014; Doaei et al., 2017; Hilman, 2015; Subramaniam & Wasiuzzaman, 2018). Therefore, diversification strategies has been the choice of certain companies in different parts of the world (Benito-Osorio, Guerras-Martín, & Zuñiga-Vicente, 2012). However, the evidence shows that success cannot be guaranteed by diversification strategy, and the achievement and failure records of various diversified organizations all over the world call for refined investigation into the issue of diversification strategies (Kruehler, Pidun, & Rubner, 2012). There is a considerable number of studies conducted on the relationship between diversification and performance in different fields (Elif, 2015; Etemad & Joker, 2016; Mehmood, 2015). However, researchers are still undecided regarding the effect of diversification strategies on performance (Asif, & Akhter, 2019; Asrarhaghghi, Rahman, & Sambasivan, 2013; Benito-Osorio et al., 2012; Marinelli, 2011). The inconsistent results on this area to some extent indicate vagueness and complexity associated with it.

The impacts of corporate diversification on corporate value can be divided into three categories. Firstly, there is evidence that indicates corporate diversification in general will lead to a reduction of overall firm value (Aggarwal & Samwick, 2003; Berger & Ofek, 1995; Hoechle et al., 2012; Li et al., 2019). Secondly, firm value increasing effect due to corporate diversification (Choe, Dey, & Mishra, 2014; Ishak & Napier, 2006; Villalonga,

2004). Thirdly, there is no impact at all (Zahavi & Lavie, 2013; Pastricia & Datsgir, 2016; Subramaniam & Wasiuzzaman, 2018). Additionally, others argue that diversification will neither enhance performance nor reduce risk because a firm may diversify into areas it has less competitive advantage and that the impact of diversification depends on whether it is sectorial, geographical and industrial diversification (Acharya, Saunders, & Hasan, 2002; Hilman, 2015). Likewise, the performance of related and unrelated diversification strategy also remained an unresolved puzzle for the past few decades (Lahovnik, 2011). A large group of researchers recommended that related diversification strategy performed better than unrelated diversification (Mehmood & Hilman, 2013; Almudena, 2016). Correspondingly, there are substantial studies saying that unrelated diversifiers outperform related diversifiers (Park, 2010; Yaghoubi, Abidin, & Yaeghoobi, 2011; Patrisia & Datsgir, 2016)

On the other hand, some believe that diversification may lead to agency problem between the controlling managers and the shareholders, when management diversify in order to get personal benefit at the expense of shareholders interest (Ataullah, Davidson, Le, & Wood, 2014). Scholars have been studying the subject of diversification strategies with different samples, data sources and analytical techniques (Almudena, 2016; Benito-Osorio et al., 2012; Doaei et al., 2017; Mehmood & Hilman, 2013; Ooi, Hooy, Puad, & Som, 2014). Accordingly, previous studies has improved on research designs and measurement models, nevertheless, the evidences of inconsistent and inconclusive findings on diversification strategies – performance relationship call for more research into the topic. This study therefore seek to address some of the theoretical and managerial issues with a view to offer

solutions and recommendations based on the subsequent findings of the research work, by focusing on the Malaysian public listed companies.

1.2 Problem Statement

The global financial meltdown has exposed many weaknesses in running the affairs of companies all over the world (Hussaini, 2019). This is coupled with several accounting scandals and failures (e.g., Enron, Global Crossing, Xerox, and WorldCom), which have made a lot of investors lose confidence and, consequently, raised serious concern about the credibility and reliability of financial reports and the audit committee effectiveness in protecting investors' interests (Adegbite & Adegbite, 2012; Domikowsky, Bornemann, Duellmann & Pfingsten, 2014). In response, there has been a global transformation towards promoting and implementing governance mechanisms to minimize the opportunistic behaviors that have dented the shareholders' reliability in financial information. For instance, the United Kingdom's Financial Reporting Council had consistently reviewed the Combined Code in 2010 and 2012 and the United States in 2002 introduced the Sarbanes-Oxley Act (SOX) as a response to the scandals of Enron and WorldCom to help promote the quality of information and improve financial reporting (Kingsley, Gina & Vivian, 2014). Therefore, there is an increasing need to be more proactive in corporate governance issues since weak corporate governance can lead to the failure of a country's economic structure (Aina & Adejugbe, 2015).

Consequently, in Malaysia, series of detrimental transactions were reported within the Malaysian business cycle (Maigoshi, 2017). A typical example of these transactions is the case of United Engineers (Malaysia) Bhd (UEM). UEM acquires 32.2% interest of its

financially distressed parent company (Renong) at an inflated cost of 2.34million Malaysian ringgits. This transaction was interpreted as a deliberate effort to bailout the parent company from its financial turmoil (BusinessWeek, 1998). Another example of detrimental transaction is the case of Genting Malaysia Bhd. The subsidiary (Genting Malaysia resort world) bought a property from its parent (Genting Bhd). The issues of concern were the appointment of the same valuer by both parties and the position of the independent directors been members of the board of both companies. Analyst regarded the transaction as cash extraction by the parent company (Wahab et al., 2011).

In addition, earth-shattering dominance and participation of major shareholders in company management in Malaysia have allowed some of them to act in their own interests, leading to corporate misbehaviors (Khoo, 2003). This has adversely affected the performance of Malaysian PLCs, leading to financial distress (Maigoshi, 2017). In addition, a number of corporate collapses occurred, such as Perwaja Steel, Berhad, Renong Berhad, and KFC Holding Berhad, due partly to the lack of effective corporate governance mechanisms (Haniffa & Hudaib, 2006). This implies that poor corporate governance contributed to the corporate financial crisis in Malaysia (Fauziyah, Yusuf & Idris, 2012).

Moreover, recent studies on corporate governance shifted attention from the initial agency problem (principal-agent) to new dimension of agency problem between controlling shareholders and minority holders (principal-principal or type II agency problem) (Maigoshi, 2017) (see for example Ishak, 2004; Fraile & Fradejas, 2014; Jameson et al., 2014, Song, Wang & Cavusgil, 2015). Type II of agency problem arises as a result of concentrated ownership that is prevalent in emerging economies. In this economy most of

the listed companies are significantly owned by an individual, group of families or the state (Loon & De Ramos, 2009; Morris et al., 2011). In most of these types of business models, there is no separation between ownership and control. There, the diversification value can be infected with conflict of interest between controlling and minority shareholders. A listed subsidiary could deposit its excess value with unlisted parent for a long period, instead of diversifying the fund in order to generate interest income to both controlling and minority shareholders (Maigoshi, 2017).

The growth in corporate governance literature expresses concerns about the importance of having good governance in a corporation (Fauziyah, Yusuf & Idris, 2012). However, studies conducted on the relationship between corporate governance and firm value were accompanied by mixed findings (Castaner & Kavadis, 2013; Berger, Imbierowicz & Rauch, 2016; Khan, Tanveer & Malik, 2017; Latif, Bhatti & Raheman, 2017; Baugh, Ege & Yust, 2018; Dionne et al., 2018; Latif, 2018; Antonio, Laela & Darmawan, 2019). However, the existence of inconsistent relationship between corporate governance and firm value will not be far-fetched from the use of different proxies, methodologies, samples, and techniques to gauge the effects of corporate governance on firm value. Most of the researches in the area of corporate governance were conducted in developed economies, as rich data is available for these economies where active market for corporate control exists (Knut, 2016). There are good reasons to postulate that the effectiveness of corporate governance might be quite different in developed and emerging markets (Saravanan, 2012). Hence, studies on the area of relationship between corporate governance and firm value in the context of emerging nation like Malaysia is essential to get better understanding of the issue, since sufficient study in this area is still needed.

From the theoretical perspective, the empirical findings on how paramount the corporate board mechanisms are to be structured to boost corporate performance and serve the interest of shareholders using diverse theoretical views remain inconclusive (Combs, Perryman, & Donahue, 2007). Correspondingly, Jackling and Johl (2009), Ishak (2004) and Arosa, Iturralde, and Maseda (2010) proclaim that one theory alone cannot adequately explain the firmness of corporate governance mechanisms, thus integrating multiple theories may provide better understanding of dynamism of corporate governance.

On the other hand, prior studies on diversification and diversification value relationship have been multidirectional. It has either focused on examining the effect of diversification on firm value or on comparing related diversification strategy with unrelated diversification strategy on different performance measures. However, the findings of research in these areas remain an unresolved puzzle (Asrarhaghghi et al., 2013; Mehmood, 2015; Patrisia & Datsgir, 2016; Vogl, 2018; Li et al., 2019). Although past research studied the topic using variety of methodologies but there has been limited research on the topic for Asian economies compared to Western ones (Hilman, 2015).

As regards features of Malaysian corporate sector, Malaysia has been characterized by presence of high percentage of product diversified companies (Ahmad, Ishak, & Manaf, 2003; Doaei et al., 2014). Particularly, among private companies, diversified business groups are the most prominent corporate houses operating across a diversified choice of segments across various sectors such as manufacturing, industrial products, trading and services, construction, property investment and plantation. Study of Claessens et al. (1998), based on nine East Asian countries found that 70% of Malaysian companies reported

multiple segments in their annual reports which was second to 72% for Singapore. Ishak and Napier (2006) also reported significant diversification at around 55% for Malaysian PLCs in 2000. Similarly, recent study of Doaei et al. (2014) also shows significant level of international diversification for Malaysian companies.

Meanwhile, scholars have reported that these levels of extensive diversification from Malaysian PLCs might have resulted in misallocation of investments in less profitable and more risky business segments (Hilman, 2015). Amidst, importance of carefully selecting the level of diversification for the companies (Duru & Reeb, 2002; Geringer et al., 2000) has as well been highlighted by scholars. It is noted that companies usually might go for product diversification for getting benefits of internal capital market. But, past research on product diversification and performance relationship conducted for Asian countries, including Malaysia have inconclusive results. In this regard, certain researches revealed that diversification strategy negatively impacted performance or it was not beneficial strategy in certain ways (Lins & Servaes, 2002; Tongli, Ping, & Chiu, 2005) which is contrary to arguments of internal market efficiency.

Most importantly, given the fact that there is a huge percentage of diversified PLCs in Malaysia, though few studies are available on impact of product diversification on performance, but research into interaction impacts of the two strategies on corporate performance for Malaysian PLCs is extremely limited (Doaei et al., 2014; Yaghoubi et al., 2011) which indicates an important research gap. Hence, research into this area is warranted.

For all intents and purposes, certain scholars contend that diversification and firm value relationship need to be examined through a perspective by incorporating the impact of moderating variables, which might really influence the nature of this relationship (Martínez-Campillo, 2008; Mehmood & Haim, 2013; Ravichandran, Han, & Hasan, 2009). Although, prior studies incorporated certain moderators (such as corporate parenting, market structures, control system and managers wealth maximization) into this relationship (David et al., 2010; Li & Rwegasira, 2008; Markides & Williamson, 2007; Martínez-Campillo, 2008) but there have been limited studies utilizing corporate strategy issues such as managers' wealth maximization as moderator into the relationship in other countries (Choe et al., 2014). While the study is most requiring in the Malaysia context, hence justifies the purpose to undertake this study.

Despite the attention paid to diversification as a corporate strategy, the relationship between decisions on firm boundaries and the compensation of the firm's top managers has remained warranted in the Malaysian context. Agency theory provides a different perspective on strategic scope decisions, proposing that managerial decisions regarding the scope of the firm may be less than optimal due to conflicts of interest between the agents (managers) and the principals (shareholders). Proponents argue that the separation of ownership (embodied within the "principals") and management (embodied within "agents") can result in the expropriation of firm value (agency costs) by said agents (Adner & Zemsky, 2016).

Corporate diversification can work to the benefit of managers at the expense of shareholders in a number of ways. Managerial compensation, for example, increases with

the firm's size and strategic scope (i.e., higher levels of diversification), though such higher diversification levels may not necessarily result in improved profitability (Jensen, 2010). Furthermore, the risk of total firm failure is reduced in a diversified firm, and thus managerial employment risk is subsequently reduced. Scope decisions made under circumstances such as these impose agency costs on the firm, in that diversification activities driven by such motives serve managerial financial self-interests (higher compensation and job security), while providing no financial benefit to shareholders (Wiersema & Beck, 2017). Then there is the concept of "managerial entrenchment" (Mehmood, 2015). Managers may specifically direct diversification activities into businesses that increase the firm's dependence on said managers' particular skills, thus increasing the firm's dependence on them as specific individuals. Personal position, again, is enhanced at the expense of shareholders.

A final example is in the agency cost of free cash flows (Jensen, 2010). Cash flow in excess of the amount sufficient to fund all positive net present value opportunities presents a temptation to managers. Arguably, that excess cash flow should be returned to shareholders, to do with as they see fit. Such a course of action would, however, represent a dilution of managerial power by reducing the amount of resources under managerial control. Diversification into a line of business with a negative net present value, while detrimental to shareholders, presents managers with a means through which to retain control over said resources.

The essence of the agency theory argument is that there are many ways in which managers can benefit from a strategy of diversification (even if shareholders do not). Managerial

opportunism and the existence of free cash flows are thus seen as significant motivating factors underlying decisions to pursue corporate diversification. Appropriate corporate governance structures, through which managers are effectively monitored, as well as incentivized compensation schemes, through which managers' interests are aligned with those of shareholders, can reduce such agency costs. Since managers are face with various motives of corporate diversification. They might decide to go for the intention that favors their personal interest at the detriment of the shareholders. However, when the outcome of their decision is being incentivized with monetary benefits, they will be compelled to undertake a diversification strategy that will eventually lead to an increase in shareholders wealth and firm value. Thereby, maximizing their own wealth and or benefit. However, this study aims to further validate the aforementioned claimed by investigating the effects of diversification strategies (related & unrelated) on firm value by taking managers' wealth maximization role as the moderator in the relationship.

1.3 Research Questions

In an attempt to address the problems, that have been identified, this study seeks to answer the following research questions.

1. Do corporate board mechanisms influence the diversification value of publicly listed companies in Malaysia?
2. Do corporate diversification strategies influence the diversification value of public listed companies in Malaysia?
3. Does wealth maximization moderate the relationship between corporate diversification strategies and diversification value of PLCs in Malaysia?

1.4 Research Objectives

The main objective of this research work is to assess the relationship that exists between corporate board, diversification strategies and firm value of listed public firms in Malaysia.

The specific objectives are as follows.

1. To study the relationship between corporate board mechanisms and the diversification value of public listed companies in Malaysia.
2. To examine the influence of corporate diversification strategies on the diversification value of public listed companies in Malaysia.
3. To determine the moderating effect of wealth maximization on the relationship between corporate diversification strategies and diversification value.

1.5 Scope of the Study

This study focuses at assessing the relationship between corporate board, diversification strategies, manager wealth maximization and the value of diversified public listed companies. The study is limited to public limited companies listed in the Stock Exchange, Bursa Malaysia. The period covered by the study is for the year 2017, the single year period is considered adequate to generate sufficient data for corporate diversification related study. This is also in consistent with the work of Ishak (2004), Lins and Servaes (2002), Goddard, Molyneux and Wilson (2004) and Miller (2006). A short time period is desirable because strategic plans frequently changes overtime, (Eukeria & Favourate, 2014, Mehmood, 2015), therefore in diversification studies, a shorter time period is desirable (Daud et al., 2009).

Another explanation for relying on 2017 years data is in relation to the introduction of the MCCG 2017 codes which supersedes the 2012 MCCG. The new MCCG introduces substantial changes and recommendations with a view of raising the standards of corporate governance of companies in Malaysia. The MCCG now employs the CARE approach (abbreviated from the term 'Comprehend, Apply and Report') by shifting from the 'comply or explain' method in the 2012 code to a 'apply or explain an alternative' method. This is believed to allow greater flexibility in the application of the best practices.

The new MCCG also adopts a proportionate application to companies depending on size, complexity and suitability. While the MCCG applies to all listed companies in Malaysia, certain practices are only applicable to 'Large Companies', which are companies on the FTSE Bursa Malaysia Top 100 Index or companies with market capitalization of RM2 billion and above at the start of their financial year. In addition, the MCCG now expressly encourages non-listed entities including state-owned enterprises, SMEs and licensed intermediaries to embrace the MCCG to enhance accountability, transparency and sustainability.

Companies are now required to provide a meaningful explanation in their annual reports on the manner in which the practices are applied and, where alternative practices are adopted to meet the Intended Outcome, to provide reasons for such alternatives and where appropriate, the timeframe required for its implementation. The first set of companies required to report on conformance with the MCCG in their annual report are companies with financial years ending 31 December 2017.

In addition to the justification for the selection of year 2017 is based on the newly introduced 2016 companies act which supersede the previously used of companies act of 1965. The new companies act of 2016 came up with various changes and reforms, some of which are; prescribes the minimum number of directors for a public company is two resident directors, provides that the fees of the directors, and any benefits payable to the directors of a public company, or of a listed company and its subsidiaries, shall be approved at a general meeting, abolish the maximum age for directorship, enhance internal control, corporate governance and corporate responsibility, statutory declaration by promoters / directors to be replaced with statement of compliance.

The year 2017 was chosen as it was the latest financial year for which all listed companies' published annual reports were available at the time when data collection was started after the gazette of the 2016 companies act. PLCs have a few months after their financial year-end to publish their audited annual report, data for 2018 could not be collected since not all companies' annual reports ended in 2018 were available at the time of data collection.

The study collects corporate level secondary data for its analyses, whereas, the data are collected through company annual reports, and World scope DataStream among others. The findings that are obtained through this research is applicable to all diversified companies in general and Malaysian PLCs in particular. The methodology presented in Chapter 3 as well as discussions made in Chapter 4 further magnify the scope of this study.

1.6 Significance of the Study

This study demonstrates the importance of selecting corporate board, related and unrelated diversification strategies, manager's wealth maximization and their possible combined effect on corporate performance. It is anticipated that an appropriate combination of a particular diversification strategy and managers' wealth maximization will have a positive effect on corporate value. The theoretical and practical significance of the study is evident on the basis of the following discussions.

1.6.1 Theoretical Significance

This study address important issues and existing gaps in the literature concerning the interaction between corporate board, diversification strategies and the performance of diversified public listed companies. Although there are certain number of studies examining the effects of corporate board and diversification strategies on corporate performance, there is limited research on the interrelationships between corporate board, diversification strategies and firm performance in an emerging market like Malaysia (Hilman, 2015; Ishak & Manaf, 2013). Most remarkably, there was a research gap in terms of absence of research (to the best of the researchers' knowledge) on the moderating effect of managers' wealth maximization in diversification and performance relationship of diversified PLCs in Malaysia. Hence, this study intend to fill the research gap by combining together factors of strategic importance, such as diversification strategies (related & unrelated), wealth maximization and firm value into same research framework.

In this regards, this study explore the relationship among crucial variables of strategic nature and contribute to the relevant body of knowledge. Specifically, this study contributes to the body of literature on corporate board, diversification strategies and corporate performance. In addition, this research work also contributes to sets of studies that examined diversification strategies and firm value relationship from the perspective of moderating variables (Choe et al., 2014; Mehmood, 2015; Li, 2007; Ravichandran et al., 2009). Similarly, the study utilize some of the suggestions recommended by those scholars (Mehmood & Hilman, 2013) with regards to studying the relationship of these variables using certain moderators.

Moreover, the findings of this research work may contribute to the theoretical perspective underpinning this study (i.e. by supporting their postulations), such as the agency theory, resource dependency theory, stakeholders' theory, transaction cost economic and market power view. Based on the agency theory, it was assumed that the agent has more information and knowledge on the firm's operations as compared to the principal (Adams, 1994). Although, Mat Rabi et al. (2010) revealed that in order to stop the agents from maximizing their self-interest, having good corporate governance practices through effective monitoring and control could reduce the managerial opportunism, especially in making decision on diversification strategies. On the other hand, the basic premise of resource dependency theorists, is that corporations depends upon one another for access to valuable resources and therefore, seek to establish links in an attempt to regulate their interdependence (Hung, 1998; Marinelli, 2011).

Since diversification is being guided by resources and capabilities of an organization (Wernerfelt, 1984). Consequently, the organization diversifies into similar or different industries if it possesses excess resources and capabilities that it could utilize profitably in those industries (Martin & Sayrak, 2003). Thus, related and or unrelated diversification becomes more rational in markets where sale of excess resources and proficiencies outside the organization conveys significant transaction costs and therefore diversification becomes the best way to utilize them within and outside the organization (Goddard, McKillop & Wilson, 2008).

1.6.2 Practical Significance

Several features of this research point towards its practical significance. Most importantly it is noteworthy that limited researches were conducted in the context of Malaysian corporate sector (Daud et al., 2009; Ishak & Manaf, 2013; Mehmood & Hilman, 2013). Though, Malaysian corporate sectors play an immense role in the growth and development of national economy. Therefore, further studies needs to be conducted that will provide valuable recommendations to Malaysian corporate managers in particular. In addition, this research studies the effects of corporate governance, diversification strategies (related & unrelated) on the value of diversified Malaysian public listed companies. The prominence of this research signifies from this point that study certain factors which are consider to be of strategic importance for any public listed companies. Similarly, this study also examines the moderating effect of managers' wealth maximization roles on diversification strategies and diversification value.

Therefore, the interrelationships that were explored between corporate governance, diversification strategies, and diversification value based on the data generated from PLCs in Malaysia may have its significance to Malaysian PLCs in particular. The recommendations given as a result of this study may improve their managerial decision making. The findings may also assist Malaysian CEOs, directors and corporate planners to get rid of the dilemma on their choice of the best and most profitable diversification strategies. Particularly, the understanding gained in the study regarding the relationship between diversification strategies and wealth maximization motive in apprehending the effect and using most appropriate strategy for adding value to their business.

Although, Malaysia has successfully come out of the 2008-09 global financial crises but the economy is faced with external environment challenges in maintaining its growth targets (IMF Staff Country Report, 2012, as cited in the study of Mehmood (2015). The discussions and recommendations that was provided in this research may offer useful insights in managerial decision making on relevant issues, for Malaysian board composition and diversification strategists in particular and other managers in general. As a result, it may help to improve the performance of Malaysian corporate sectors. Additionally, Malaysian PLCs pay significant contribution to its GDP. The recommendations that was provided through this research work regarding important corporate strategy issues may help these sectors improve their contribution to Malaysia GDP. This would ultimately facilitate in achieving the target of GDP growth rate for certain periods. The findings from this study may also serve as a guide for capital investment decisions made by corporate sectors on investing in related or unrelated sectors and industry segments which in turns might help achieve better economic balance.

1.7 Structure of the Thesis

This research thesis is been structured into five chapters, the first chapter captured the introductory aspect of the study which was discussed above. While the second chapter which is also known as the literature review aspect begins with different concepts and approaches of corporate governance including historical antecedents, definitions, mechanisms, and other related empirical studies. In addition, the chapter review important concepts on corporate diversification and financial performance which are also focal areas of the study. The chapter further review different concepts and approaches linking corporate governance, diversification and firm value. In this regards, different philosophies and scholarly views were highlighted and discussed. Therefore, the chapter explore discussions on the assumptions of the theoretical underpinning of the study. The variables of the study were also identified and interpreted based on related works from prior researches.

The third chapter (methodological aspect) of the thesis deliberates on aspects of research methods that is applied in this study. As a result the chapter starts with the theoretical framework of the study which depicts the link between all the explanatory variables, moderating, and depended variables of the study. This was followed by the research hypothesis which metamorphosed from the earlier stated research questions. The chapter further deliberates on the control variables of the study, as well as the research design. The section that follows then concentrates on the operationalization and variable measurement,

population and sampling, method of data collection and analysis as well as the model specification.

Chapter four presents the analyses and discussion of the objective of the study, which is the relationship between corporate boards, corporate diversification and firm value. The chapter begins with explanation on the sampled firms and sampling adequacy. This is followed by discussions on the results of descriptive statistics, moderating, explanatory and control variables. The next section presents the correlation analysis of the study. The multiple regression part of the chapter discusses the results of the multivariate regression diagnostic tests and the results of the estimation model. Finally, the chapter concludes with robustness test to check for the sensitivity of the main regression analysis.

Chapter five is mainly devoted for conclusions and discussions on the results obtained in chapter four. Additionally, it discusses implications of the study and its limitations, and presents recommendations for the future research into relevant areas.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

This chapter contains a review of prior studies on corporate governance, diversification strategies, diversification value and managers' wealth maximization. The chapter also provides a discussion on the concept of corporate governance and corporate diversification. In addition, the chapter evaluates different approaches linking corporate governance, diversification and diversification value. In this regards, different philosophies, theories and scholarly views are highlighted and discussed. Therefore, the chapter explores discussions on the assumptions of the theoretical underpinning of the study. The variables of the study are also identified and interpreted based on related works from prior researches.

2.2 Concept of Corporate Governance

Corporate governance can be defined as standard rules and regulations, as well as internal processes of an organization that are aimed to provide guarantees for management who are interested in achieving the rights of the owners and protecting the rights of all the interested parties of the organization (Ghalboon & Khalid, 2011). It is also defined as rules, processes or laws through which companies are governed, regulated, and operated with the sole aim of promoting transparency and efficiency in the financial system and stimulating the assignment of responsibilities in an ethical, professional, and objective manner (CBN Code

of CG, 2014). Therefore, good corporate governance is pivotal in providing credible and reliable information which, in turn, enhances the confidence of the investors.

The evolution of modern corporate governance is originated from the publication of Berle and Means (1932). However, Wells (2010, p. 1251) argued that “*the concept of corporate governance has been in existence since the application of corporate firms created the feasibility of conflict between owners and managers*”. From the above, it is observed that the concept of corporate governance arises because of the separation between ownership and control which brings about agency problems in organizations. Thus, the agency problem depicts a conflict of interest between the shareholders and management. Hence, the concept of corporate governance is an act of making sure that companies continue to establish a means for investors to carry out corporate risk and produce wealth without inflicting fraud or any type of abuse on the investors and stakeholders (Watts & Zimmerman, 1983; Wells, 2010).

Several corporate and accounting scandals and failures (e.g., Enron, Global Crossing, Xerox, and WorldCom) raised serious concerns about the credibility and reliability of financial reports. Thus, there is a need to protect investors’ interests. In response to this, there has been a global transformation towards promoting and implementing governance mechanisms to minimize the opportunistic behaviour that have dented shareholders’ reliability in financial information. For instance, The United Kingdom’s Financial Reporting Council consistently reviewed the Combined Code in 2010 and 2012 and the United States, in 2002, introduced the Sarbanes-Oxley Act (SOX) as a response to the scandals of Enron and WorldCom, to help promote the quality of information and improve

financial reporting (Bala, Amran & Shaari, 2019). The Public Company Accounting Oversight Board (PCAOB) has also been introduced to supervise and oversee the audit of the US public companies thereby protecting the interests of investors and enhancing the independent audit report which will, in turn, improve the informativeness of the earnings (Jackson, 2010).

2.4 Corporate Governance in Malaysia

The major sources of corporate governance reforms agenda in Malaysia are not far fetch from the Malaysia Code of Corporate Governance (MCCG) by Finance committee on Corporate Governance, Security Commission and Financial Sector Master Plan, Capital Market Master Plan and Bank Negara Malaysia on the financial sector. The MCCG provides guidelines on the principles and best practices in corporate governance and the direction for the implementation as well as plans the future prospects of corporate governance in Malaysia.

2.4.1 Malaysian Code on Corporate Governance (MCCG)

The Malaysia MCCG was first introduced in the year 2000, drawing significant lessons from the 1997/1998 Asian financial crisis to strengthen the corporate governance framework and increase investors' confidence. The crisis exposed a number of corporate governance weaknesses many South-East-Asian corporations, and Malaysian listed companies are not an exception. Most of the Malaysian companies have been identified with lack of transparency, poor minority shareholders' protection and allegations of cronyism (Hassan Che-Haat, Rahman & Mahenthiran, 2008; Wahab, How & Verrhoeven, 2007).

The finance committee on corporate governance (FCCG) identifies the importance of corporate transparency through improved financial disclosure and the increasing role of institutional investors' activism. FCCG believes that for Malaysia to catch-up with emerging global competition, corporate governance problems have to be resolved amicably (MCCG, 2000). Based on this, FCCG recommends for the establishment of the MCCG together with minority shareholders watch dog group. These recommendations are made to install corporate governance best practice in Malaysian firms and protect minority shareholders from insider-dealings (Wahab et al., 2007).

2.4.2 Malaysian Code of Corporate Governance 2000 (MCCG 2000)

The FCCG's recommendations of 1999 lead to the establishment of the first set of MCCG in 2000. The MCCG 2000 has been substantially clued from Cadbury and Greenburg codes, but more inclined to Hampel corporate governance disclosure approach. Public listed firms in Malaysia are recommended to disclose in their annual reports the extent they have complied with the Code. Whether the Code is effective for Malaysian firms is an important issue that requires immediate attention as the Code may not really reflect the environment and culture in Malaysia (Ishak, Amran & Abdulmanaf, 2017). Hampel committee recommends for a hybrid approach to disclosure of corporate governance codes. This approach takes some elements of both prescriptive and non-prescriptive to corporate governance approaches. The prescriptive approach requires reporting entities to disclose their compliance with the stated desirable governance practice principles in their financial reports. On the other hand, non-prescriptive approach preferred narrative disclosure of the corporate governance practice adopted by reporting entity. This approach takes into

cognizant the peculiarities of some companies and believes that directors should design the appropriate governance best practice that best suit their entity.

To overcome the shortcomings of both approaches, Hampel committee re-emphasizes the need for principles that firms have to comply with and disclose in their financial reports. However, the committee recommends the directors to some narrative disclosure in the financial reports on how relevant principles are applied in their respective companies. This approach is aimed at securing sufficient information disclosure that will enable investors and other stakeholders to assess the performance and corporate governance practices of reporting entities and take informed economic decisions accordingly. FCCG has recommended that MCCG 2000 be categorized into four parts.

The first part of the MCCG 2000 set out governance principles for all Malaysian registered firms. The recommendation permits listed firms to apply these principles flexibly and taking into account their varying nature. Narrative disclosures are required in the financial report on how each listed company applies principles that are relevant to their business circumstances. This is to secure sufficient disclosure so that investors and others can assess companies' performance and governance practices, and respond in an informed way.

The second part sets out best practices for companies. It identifies a set of guidelines or practices intended to assist companies in designing their approach to corporate governance. While compliance with best practices is voluntary, companies will be required as a provision of the listing requirements to state in their annual reports, the extent to which they have complied with the best practices set out in the part and explain any circumstances justifying departure from such best practices. The third part of the recommendation also

known as ‘exhortations to other participants’, is not addressed to listed companies but to investors and auditors to enhance their role in corporate governance. These are purely voluntary. While the last aspect of the requirements provides explanatory notes to the principles and best practices set out in parts 1 and 2 and exhortations set out in part 3. Additionally part 4 also sets out best practices directed at listed companies that do not require companies to explain circumstances justifying departure from best practices “mere best practices”.

2.4.3 Malaysian Code of Corporate Governance 2007 (MCCG 2007)

The introduction of MCCG in 2000 has improved corporate governance mechanisms in Malaysian corporations (Wahab et al., 2007). However, in 2007, MCCG have been reviewed by the securities commission and approved by high-level FCCG effective from 1st October 2007. The primary aim of the MCCG reviewed is to improve the quality of the listed companies’ board and maintain the existing investors’ confidence in the Malaysian capital market (Badawi, 2007). The eligibility for appointment as director, the role of the nominating committee, qualification for appointment as of audit committee, composition of audit committees, frequency of meeting of the audit committee, internal audit unit and their reporting chain are the major areas affected by the amendment. The review did not affect the first part of the MCCG 2000, rather, are more on the second part of it that is the best practice.

The revised code provides clear direction on the areas that nominating committee should take into account while assessing the candidate’s eligibility for directorship. This is done to improve the competency and efficiency of the board members in the discharge of their

corporate oversight and control. The reviewed code also requires the nominating committee to document the assessment and evaluation process undergone properly while recommending any candidate for directorship including independent non-executive directors. Minutes of board meetings should cover, not only the decisions arrived at, but also the issues discussed before arriving at such decision.

On the audit committee, the MCCG 2007 provides that membership of the audit committee should be exclusively for financially expert non-executive directors. The frequency of meeting with the external auditor without the present of executives has been increased to at least twice in a year. Moreover, the finance director, the head of the internal audit unit and representative of the external auditor should attend the meetings of the committee. The committee can invite any other board member to attend its meetings where the situation warrants. The chairman of the committee should engage with the management on all relevant issues affecting the company. The activities of the audit committee should form part of the corporate governance disclosure in the annual report of the company. The revised code mandates for the establishment of an internal audit unit in all public listed companies. Unit should be independent of the management and reports directly to the audit committee.

2.4.4 Malaysian Code of Corporate Governance 2012 (MCCG 2012)

Securities Commission Malaysia had issued a newly revised code of corporate governance in 2012. MCCG 2012 focuses on the roles of corporate directors, been responsible fiduciaries through strengthening the composition and structure of corporate boards.

Directors have the duty to direct their efforts and resources to achieve the best for the company and its shareholders without compromising the interest of other stakeholders.

They should be effective custodians and stewards of the company in setting strategic direction, effective risk management strategies, putting strong internal control in operations, compliance with relevant laws and ethical values and the rest. MCCG 2012 provides recommendations and commentary to each recommendation for a better understanding of its contents. In summary, MCCG 2012 places a sound basis for corporate boards and their committees to discharge their fiduciary duties efficiently. It also encourages balanced and timely disclosure, improves reporting quality, and stresses the importance of internal control as well as risk management in the corporations. The first principle of the MCCG 2012 requires the board to set and ensure compliance with the code of conduct and ensure sustainability in corporate operations. It also requires the board charter to be public and periodically reviewed. Annual assessment of independent directors, restriction of their tenure and justification for the extension of tenure as non-executive as the case may be, becomes part of the new code. Principle 3 (recommendation 3.5) of MCCG 2012 provides that majority of board members should be independent directors if the chairperson happens to be a non-independent director, and the board should set a time expectation that each member must commit to the company. Corporate transparency through the efficient use of information technology where possible should be part of the corporate policies. The code promotes the use of poll while voting on any matter at general meetings.

2.4.5 Malaysian Code of Corporate Governance 2017 (MCCG 2017)

A new Malaysian Code on Corporate Governance 2017 (“MCCG”) was released by the Securities Commission Malaysia and takes effect on the 26 April 2017, replacing the 2012 code. The new MCCG introduces substantial changes and recommendations with a view of raising the standards of corporate governance of companies in Malaysia. The MCCG now employs the CARE approach (abbreviated from the term ‘Comprehend, Apply and Report’) by shifting from the ‘comply or explain’ method in the 2012 code to a ‘apply or explain an alternative’ method. This is believed to allow greater flexibility in the application of the best practices.

The new MCCG also adopts a proportionate application to companies depending on size, complexity and suitability. While the MCCG applies to all listed companies in Malaysia, certain practices are only applicable to ‘Large Companies’, which are companies on the FTSE Bursa Malaysia Top 100 Index or companies with market capitalization of RM2 billion and above at the start of their financial year. In addition, the MCCG now expressly encourages non-listed entities including state-owned enterprises, SMEs and licensed intermediaries to embrace the MCCG to enhance accountability, transparency and sustainability.

Companies are now required to provide a meaningful explanation in their annual reports on the manner in which the practices are applied and, where alternative practices are adopted to meet the Intended Outcome, to provide reasons for such alternatives and where appropriate, the timeframe required for its implementation. The first set of companies

required to report on conformance with the MCCG in their annual report are companies with financial years ending 31 December 2017.

The MCCG has three (3) key Principles, each setting out the intended outcomes together with recommended practices and further explanatory notes in guidance on the implementation of such practices. Highlights of the new MCCG include:

Strengthen Independence of the Board

The 2012 MCCG code required that in cases where the chairman of the company is not an independent director, the board had to comprise of a majority of independent directors. In all other cases, there was no requirement that independent directors should constitute a majority. The 2017 MCCG now provides that at least half of the board must comprise of independent directors and, for Large Companies, there must be a majority of independent directors.

Tenure of Independent Directors

Consistent with the approach under the 2012 MCCG, the 2017 MCCG discourages an independent director from serving for more than 9 years. Retention of an independent director above 9 years will require shareholders' approval, whereas retention of an independent director above 12 years will require shareholders' approval through the two-tier voting process. The voting process can either be by large shareholders and or voting by other shareholders. Large companies are discouraged from retaining an independent director for more than 12 years. The two-tier voting requirement will be effective only for resolutions to be tabled at general meetings.

Board Diversity

The board of large companies will need to comprise at least 30% women directors. The 2017 MCCG also encourages companies in general to include women participation not only at board level but also in senior management.

Transparency in Directors' Remuneration

The 2012 MCCG requires the board to establish formal and transparent remuneration policies and procedures for directors and for these policies and procedures to be disclosed in the annual report. The 2017 MCCG now goes a step further by requiring the company to make available such policies and procedures on the company's website. The 2017 MCCG also requires detailed disclosure on a named basis of the remuneration paid to directors (this includes all fees, salary, bonus, benefits-in-kind and other emoluments), and the remuneration paid to the top 5 personnel in senior management within the bands of RM50,000 (this includes all fees, salary, bonus, benefits-in-kind and other emoluments).

It is also worth noting that the Companies Act 2016 which came into force recently introduced a new requirement for all fees of directors and any benefits payable to directors (including any compensation for loss of employment) of a public company (listed or otherwise) to be approved by the shareholders at a general meeting. The additional disclosure requirement under 2017 MCCG reinforces the need for transparency of board remuneration and accountability to the shareholders.

Strengthen Independence of Audit Committee

The chairman of the audit committee must not be the chairman of the board. It is also recommended as a step up practice for the committee to comprise of independent directors only.

Risk Management Committee

Consistent with the approach under the 2012 MCCG, companies should ascertain the risk appetite for the business by setting appropriate risk management and internal control policies. As a step up practice, it is recommended that the board should establish a risk management committee which comprises a majority of independent directors to oversee the company's risk management framework and policies and its implementation.

Participation at General Meetings

In line with the 2012 MCCG approach in strengthening the relationship between the company and its shareholders, the 2017 MCCG has introduced additional requirements to improve shareholders participation and engagement with the board at general meetings: (a) Notice of annual general meeting to be given at least 28 days before the date of meeting. The Companies Act 2016 requires only at least 21 days. (b) All directors should attend general meetings to engage with the shareholders. (c) Companies with large numbers of shareholders or have meetings in remote locations to leverage on technology to facilitate electronic voting and remote shareholders' participation.

While the key principles and recommended practices in the 2012 MCCG are largely retained with enhancements under the new 2017 MCCG, the updating of the code is aimed to reflect global principles and internationally recognized standards and practices of corporate governance. As such, adherence by companies to the 2017 MCCG will catapult Malaysian companies to be on par with international standards of governance.

2.4.5.1 Organization of the MCCG 2017

Principles

The Principles of the MCCG 2017 encapsulate the fundamentals underpinning good governance practices that companies should apply when implementing the Practices. There are four Principles in the MCCG 2017:

- ❖ Supporting board leadership and effectiveness;
- ❖ Safeguarding the integrity of financial and corporate reporting;
- ❖ Managing risks to preserve and create value; and
- ❖ Strengthening relationship with shareholders.

Practices

Practices are actions, procedures, or processes which companies are expected to adopt in order to support long term success of the company, market confidence and business integrity. The practices among others, focus on board effectiveness, protecting the integrity of financial reporting, the importance of risk management and internal controls, as well as shareholders exercising their stewardship responsibilities. In situations where the company is unable to adopt the identified practice, it must provide clear explanation for non-adoption

of the practice and demonstrate how an alternative practice which it adopts is able to fulfill the Intended Outcome.

Intended Outcome

Each practice is followed by an Intended Outcome which provides the intention, rationale and objective of each practice.

‘Apply or explain an alternative’

The MCCG has been operating on a ‘comply or explain’ basis since its introduction in 2000. While progress has been recorded in several areas of corporate governance, there is still a lot of headroom to embed stronger corporate governance culture. These include areas where companies give effect to the spirit and intention behind corporate governance practices, understand its role in supporting long term value creation and maintaining the trust between companies, stakeholders and regulators. Corporate governance weaknesses that surfaced from the surveillance and enforcement functions of the regulators reveal that companies still adopt a mechanistic approach to corporate governance, which is perpetuated by the ‘comply or explain’ approach.

Hence, the MCCG 2017 adopts a new approach - ‘apply or explain an alternative’ where companies are required to provide clear and meaningful explanation on how they have adopted the Core practices in MCCG 2017, and achieve the Intended Outcome of each practice. ‘Apply’ requires greater thought process and consideration in implementing or undertaking the practices, including in disclosing information on these practices. Companies which do not adopt the identified Core practices in the MCCG 2017 must

provide clear explanation for the non-adoption of the practice(s) and an alternative which is able to fulfill the Intended Outcome. The explanation must be reasonably detailed and informative so that the market understands how the alternative meets the Intended Outcome.

Companies should carefully consider the Intended Outcome and be guided by it in providing meaningful explanation on any alternative practices. Statements such as “the board finds the independent director to still be independent despite the 9 year tenure” does not provide meaningful explanation on how the objectiveness of the director and overall board independence has not been compromised by the long tenure. Listed companies are required to disclose and explain their application of the Core practices in the MCCG 2017 in accordance with Bursa’s Listing Requirements. The disclosure will be based on the ‘apply or explain an alternative’ approach as explained earlier.

The Core+ practices are voluntary. However, companies are strongly encouraged to adopt them and disclose in the annual report how the practices are being undertaken or implemented. Shareholders should also carefully consider the explanation provided by companies to ensure that the company is well-governed and demonstrate intention to advance their practices. Where necessary and relevant, shareholders should consider engaging companies for explanation or clarification on their policies and/or practices.

2.4.6 Capital Market Master Plan (CMP)

The first Capital Market Masterplan (CMP1) was launched in February, 2001, in order to guide the development of the Malaysian capital market for the period of 2001 to 2010. The

CMP1 provided the strategic vision for Malaysia to develop a broad and well-regulated capital market that contributed to nation building efforts. However, the second CMP2 was introduced in April, 2011, in order to compliment the mission of CMP1. The main objective of CMP2 is to “shape greater collaboration and partnership with domestic and international participants for Malaysia to achieve a fully developed capital market within the decade (i.e.2011-2020)”. In addition, the CMP2 provides equal emphasis to attain governance objectives to ensure Malaysia’s capital market continues to be properly regulated with participants strengthening their capabilities and professional standards as well as exercising strong sense of concern towards the interest of their customers in trailing growth objectives. The CMP2 as tagged, “Growth with Governance” describes the challenges for the capital market by expanding its role in stimulating national economic growth while addressing concerns about the efficacy of markets in the aftermath of the global financial crisis. Growth with governance is aimed at getting markets to work better for all stakeholders. The term governance is used to generally describe how regulation interacts with market mechanisms to distribute capital resources efficiently and justly. Therefore, governance process is enriched by extensive participation and engagement to ensure that the rights and interests of shareholders are properly safeguarded. It is consequently the main chore of regulation to ensure that governance arrangements are sufficiently robust in maintaining public confidence in the reliability of Malaysian markets.

Moreover, the presence of governance mechanisms can be considerably explained by the inclusion of the recommendations in the CMP which focus on effective corporate governance. The dimension of corporate governance as contain in the CMP among others include the strengthening of minority shareholders’ right, improving the means of

communication between companies and the shareholders, requiring shareholder value disclosures for securities issuance, enhancing the quality and independence of auditors, restructuring takeovers and merger exercise, introducing measures to enhance regulatory, accountability and transparency.

2.4.7 Institutional Development

Development of corporate governance in Malaysia is accompanied with the institutional development, includes the establishment of Malaysia Institute of Corporate Governance (MICG) and the Minority Shareholders Watchdog Group (MSWG). Additionally, with the Inauguration of Level Finance Committee on Corporate Governance, which is a non-profit public company limited by guarantee, with founding members consisting of the Federation of Public Listed Companies (FPLC), Malaysian institute of Accountants (MIA), and Malaysian Association of Certified Public Accountants (MICPA) among others.

Bursa Malaysia Berhad also participated in effort of enhancing corporate governance in Malaysia by revamping its listing requirements. For instance, Chapter (15) of the revamped listing requirements addresses issues on corporate governance and one of the foremost requirements spells that a listed issuer must ensure that its board of directors make the following statements in relation to its compliance with the Malaysia code on corporate governance in its annual report.

A narrative statement of how the listed issuer has applied the principles set out in Part 1 of the Malaysia Code on Corporate Governance to their particular circumstances; and a statement on the extent of compliance with the Best practices

in Corporate Governance which statement shall specifically identify and give reasons for any area of non-compliance with part 2 and the alternatives to the Best practices adopted by the listed issuer, if any.

The requirements was meant for the regulation of companies to be more transparent and accountable in their dealings in order to gain investors' confidence. It is hoped that this would reduce the effects of agency theory, hence paving way for more robust capital market. Ultimately, these efforts would also boost the country's economic performance as well as inspiring the inflow of foreign direct investment. In order words, good corporate governance is key to a more competitive and robust corporate sector, which in turns would lead to a more sustainable economic development.

2.4.8 The Malaysia Institute of Corporate Governance (MICG)

The sole aim of MICG is the facilitation of business and corporate development in the country through enhanced corporate governance best practices. Though, corporate governance has succeeded in attracting a good deal of public interest due to its apparent importance for the economic well-being of corporations and the society at large. Conversely, the concept of corporate governance should be defined to suit the needs of a nation because it potentially covers a large number of diverse economic phenomenon of which are different from other developing nations. However, corporate governance is not a one size that fits all.

Although, the regulators have created a creditable framework for corporate governance. Malaysian corporations are yet to achieve a satisfactory level of corporate governance

practices and compliance. This is evident from a joint study conducted by the emerging market investment bank and Asian Corporate Governance 2003 whereby the country was ranked the ninth of ten in terms of rules and regulations but only struggle to obtain an average score of 5.5 out of 10 for overall corporate governance best practices. In fact, the rules in the corporate code are only recommendations, while there is much skepticism that best practice recommendations and/or principled-based approaches are effective substitutes for more ruled based approaches. Therefore, this raises the question on whether corporate governance disclosure should be made mandatory instead of it been voluntary.

Consequently, making corporate governance disclosure mandatory may hinder the spirit or the core objective of the code, whereby companies discloses with not only to strengthen the corporate principles but more as a compliance effort. There have been evidences suggesting that companies who opted for voluntary disclosure are deemed to have gained more benefits as compared to those who disclosed in adherence to mandatory requirement (Mehmood, 2015). Accordingly, one could arrived at an assumption that in order to promote voluntary disclosure of corporate governance practice, companies should be more sensitized on the benefits they could achieve especially in terms of higher corporate performance. Even though, it has been accepted as a rule of thumb that better corporate governance practices leads to greater corporate performance, empirical studies has shown contradictory results. Consequently, a clear link between corporate governance and firm performance could not be established.

2.4.9 Minority Shareholder's Watchdog Group (MSWG)

The MSWG was established in August 2000 as a non-profit body to spearhead shareholder activism, particular among the retail and minority shareholders, in Malaysia, with the objective of preserving shareholder rights, minimize risks to shareholders and ultimately to enhance value to the capital market. In recognition of its public mandate shareholder activism, which is one of the key tenets of corporate governance. The Capital Market Development Fund (CMDF) has been supporting the MSWG since 2005. To date, the MSWG has been successful in building up their credibility by their active participation in Annual General Meetings (AGMs) and Extraordinary General Meetings (EGMs), where highlight concerns and issues relevant to retail and minority shareholders. They also led an industrial initiative for the development of Best Practices for institutional shareholders. In addition, the MSWG conducts yearly surveys of Malaysian public listed companies, such as the Directors' Remuneration Survey, Corporate Governance Survey and the Dividend Survey, and is able to provide proxy services for minority and retail investors. The MSWG is working towards becoming a fully independent and self-sustainable organization representing the rights of minority shareholders.

2.5 Theories of Corporate Governance and Diversification

2.5.1 Agency Theory

Agency theory relies on the concept of managerial principal and agent emanated from the school of economics and finance (Davis et al., 1997; Wu, 2012), that discovered the issue of separation of ownership and control in modern corporations and provided the basis to understand the agency theory assumptions, agency cost, and use of incentive and control

mechanisms (Afza & Nazir, 2014). The basic premise of the principal and agent theory, as revealed by Jensen and Meckling (1976) is a contractual engagement between principal and the agent to perform the service on behalf of the principal, which involved decision making authority being borne to the agent. More specifically, it can be seen as shareholders delegation of some responsibilities to a team of experts while keeping in mind that they will perform better for the success of their organizations. The study of Marie (2014) advocate that agency theory can be used to analyze the relative efficient of alternative institutional arrangements due to its focus on the nature of contractual relationship as demonstrated in figure 2.1.

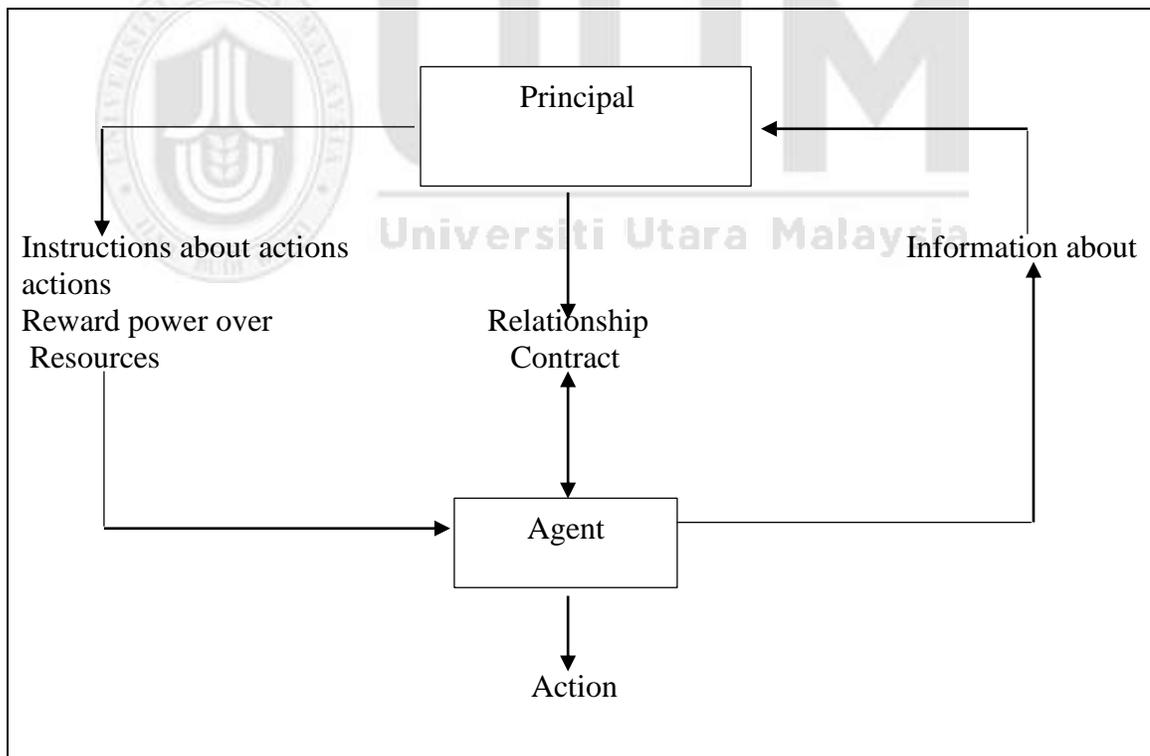


Figure 2.1 Agency Relationship
 Source: (Gray, Owen, & Adams, 1996)

Agency theory has been recognized to be the starting point of debate on corporate governance and its mechanisms (Afza & Nazir, 2014). The theory depicts people as opportunistic players who logically maximize their own satisfaction and are more concerned with extrinsic rewards at the expense of others (Hung, 1998; Mallin, Melis & Gaia, 2015). However, due to the separation of ownership from control, there might be a conflict of interest between the owner and the principal (Bonazzi & Islam, 2007). Although, both the principal and the agent seek to receive maximum benefits for the least possible expenditure, nevertheless the principal suffers agency costs when there is a variation in their interests (Muth & Donaldson, 1998; Truong & Heaney, 2013).

Besides, common benefit may neither be optimal nor even be realized due to issue of goal divergence between the parties. On the whole, agency theory laid prominence on the opportunistic behavior of managers, because the managers try to put their interest by forgoing that of the shareholders. However, Boston et al. (1996), claimed that there is a flaw in agency theorists, which tends to focus more on opportunistic agents than the opportunistic principal. Indeed, they claimed that little or no attention is given to how principals might misrepresent themselves, thereby leading to the exploitation of agents due to the fact that questions of power and authority in human relationships tend to be ignored by agency theorists. Consequently, the cost for resolving this issue increases due to the involvement of a number of corporate governance mechanisms and monitoring systems such as auditing, hiring outside directors and budgeting on the board and issuing both monetary and non-monetary benefits to managers among others (Afza & Nazir, 2014). Moreover, mutual benefit may either be optimal or even come to fruition due to goal divergence between the parties. Marie (2014) claims that it is the principal who “usually

loses out on the optimality stakes, as the theory restrictively attributes opportunism to the agent”. In this regards, Afza and Nazir (2014) concurs by stating that “corporate governance issues arise due to the misalignment of interests between the managers and investors because of the separation of ownership and control in a company”.

In accounting sceneries, agency theory is “ordinarily used to understand and predict behavior, as it assumes competing, rational , self – centered actors and focuses on contractual solutions to clashes” (Reiter, 1997). In this direction, Kunz and Pfaff (2002) revealed that “there is no doubt that agency theory and its advocated view of the firm as a complex nexus of contracts constitutes one of the major pillars of theoretical accounting”. Therefore, agency theory provides a framework for the behavior of the respective players, as a result providing a useful avenue of the practical implications for the design of governance structures (Rashid, 2015).

2.5.1.1 Agency Theory and Corporate Governance

The term corporate governance is used to understand or determine the role of agents in fulfilling major part of their contractual relationship governing agency relationships (Marie, 2014), as illustrated in figure 2.1. The basic view apprehended by agency theorist on corporate governance is that, in any given circumstance, the controlling managers may not perform to maximize shareholders returns in contrast to their personal interest, unless appropriate governance mechanisms are put in place in order to protect the shareholder’s interest (Jensen, 2010). In addition, Monks and Minow (2011) suggest that the main challenge addressed by the advocates to agency theory regarding corporate governance is not far-fetched from “how to grant managers enormous discretionary power over the

conduct of the business while holding them accountable for the use of their power’’. Moreover, the agency framework further advocates that corporate governance should be all about creating and monitoring the corporate mechanisms that are put in place by shareholders in order to control the managers to maximize shareholder wealth by mitigating agency loss (Adegbite, Amaeshi, & Amao, 2012; Bonazzi & Islam, 2007).

In general, agency theory laid more emphasis on the opportunistic behavior of managers, because they try to consider their self-interest at the detriment to that of shareholders (Afza & Nazir, 2014). Therefore, the cost of resolving this problem upturns due to the involvement of several corporate governance mechanisms and other monitoring systems and the dashing out money and monetary benefits managers among others. Additionally, Eisenhardt (1989) and Howlett (2014) revealed that the incentive schemes given to managers may assist to maximize shareholders interest and also the introduction of outcome based incentive contract that reduce managerial opportunism, especially when the CEO has the interests with the shareholders through more suitable designed incentive plan. Though, contradictory views still exists on this issue. Some scholars consider managerial compensation as part of agency problem. They allude that it pave way for more power to agents and that it tends to be a partial solution to agency problem (Bebchuk & Fried, 2009). The study of Frydman and Saks (2010) further revealed that an alternative remedy that could remove all these issues is to create a relationship between compensation and firm performance in a form of pay for performance.

2.5.1. 2 Agency Theory and Corporate Diversification

The agency theory presents a different view on corporate diversification (Montgomery, 1994; Zhao, Hwang & Low, 2013). Base on the contributions from the study Amihud and Lev (1981), several authors consider agency problems as the reasons for diversification discount (Afza & Nazir, 2014; Hoechle et al., 2012). Agency theory is based on the analysis principal and agents conflicts (Jensen, 1986; Wu, 2012). The concept of this theory implies that risk averse managers do not pursue diversification for the benefit of the organization but rather go for decisions in order to reduce the threat of professional reputation or loss of job, resulting in agency cost (Hoskisson & Hitt, 2011) or possible diversification discount (Mehmood, 2015). Accordingly, managers might be too desperate to implement diversification strategies (related and unrelated) as it might provide them with more incentives, compensation as well as control over resources and also assist them to stabilize the company's earnings and reduce the chances of bankruptcy for their own personal gains (Aggarwal & Samwick, 2003).

The agency cost tends to be high when principal does not share common interests with the agent as well as being unaware of the activities of the agent (Nyberg, Fulmer & Gerhart, 2010). However, this cost could be reduced through alignment of managerial incentives and or effective monitoring and control by the principal (Bryant & Davis, 2012). In contrast to the agency theory, the stewardship theory proposes that the managers do not always act against the sole interest of the corporation, but rather, certain managers acting as stewards are socially driven and tend to increase firm performance through a more beneficial diversification decisions (Martínez-Campillo & Fernandez-Gago, 2008; Miller & Sardais, 2011).

2.5.2 Resource Dependency Theory

Resource dependency theorists trace their origins back to the school of sociology (Joslin & Müller, 2016). When working with corporate governance, these theorists tend to focus on the linking role of the governing board to other organizations (Hung, 1998; Rashid, 2015). The basic premise of resource dependency theorists as stated by Hung (1998, p. 107) is that:

Corporations depend upon one another for access to valuable resources and therefore seek to establish links in an attempt to regulate their interdependence. An interlocking directorship is one form of links in that complex chain of connections among organizations.

The “model of man” as posited by resource dependency theorists is part of a networking directorship chain (Hung, 1998) and “who is in a position to exercise major influence over the decisions and policies of these large companies” (Useem, 1980). Business organizations use their boards of directors as a means of accessing or absorbing significant interdependent external organizations (Mehmood, 2015). This networking or interlocking directorship chain, therefore, “involves exchanging some degree of control and privacy of information for some commitment for continued support from the external organization” (Bryant & Davis, 2012). Resource dependency theorist focus on “corporate governance” is based on the assumption that “board size and composition are not random or independent factors, but are rather, rational organizational responses to the condition of the external environment” (Scott, 2015). Studies have shown that using “the well-established paradigm of inter-organizational relations, investigations have portrayed interlocking directorship

ties as a corporate strategy for improving (and reducing uncertainty) their sales, purchases, credit and public reputations” (Drees & Heugens, 2013).

2.5.2.1 Resource Dependency Theory and Corporate Governance

The key idea conveyed by the literature on corporate governance, when addressed from a resource dependency theoretical viewpoint, is that its meaning is connected with the structure of the organization in relation to other such structures and the positioning of these in the wider society. As stated by Hung (1998) “corporations depend upon one another for access to valuable resources and therefore, seek to establish links in an attempt to regulate their interdependence”. According to Hillman, Withers and Collins (2009) the board of directors can be seen as a linking instrument between the organization and the external environment.

The resource dependency theory assumes that the firm is embedded in its environment and depends on the resources from that environment to survive. The theory provides a theoretical basis for the role of corporate directors in the provision of resource and advice (Maigoshi, 2017). Unlike the agency theory which assumes the main role of directors is monitoring, resource dependency theory provides that the main role of corporate directors is the provision of resource function (Pugliese, Minichilli & Zattoni, 2014). The theory provides that the effectiveness of the board depends on the external resources that external directors are able to bring to the board for the benefit of the firm.

Under the resource dependency theory, the board of directors is useful as they provide the firm with important resources at lower costs and mediate the firm with external

environment (Withers & Collins, 2009; Davis & Adam Cobb, 2010; Chen, 2014; Tate & Bals, 2018). Pfeffer and Sancik (1978) argue that directors provide four benefits to firm: i) provision of advice and counsel, ii) channeling of information between firm and the external environment, iii) preferential access to resources, iv) legitimacy. However, Hilman and Dalziel (2003) states that firms benefit most from directors when director provide both monitoring and resource functions. The theory assumes that directors with vast industry and business knowledge and multiple directorships are saddled with the responsibility of counsel and advice as they possess the requisite knowledge, expertise and experience to handle the duties (Maigoshi, 2017). Therefore, well-diversified large boards handle the duties effectively (Castro, De La Concha & Perinan, 2009; Maria, Stock, Zacharias & Schnellbaecher, 2017).

This study attempts to identify the connotative meanings and theoretical bases used by academic writers in the study of corporate governance. It is evident from the literature that connotative meanings given to the term “corporate governance” vary depending on the theoretical viewpoint of the researcher. Indeed, both the agency theorists and resource dependency theorists convey a different meaning when using the term “corporate governance”. As revealed by the literature, there is a considerable divergence of opinion as to what “corporate governance” can mean, although it should be noted that those writing from an agency theory perspective dominate the literature (Marie, 2014). However, the agency theory alongside the resource dependence theory are used as part of the theory underpinning this research study.

2.5.2.2 Resource Dependency Theory and Corporate Diversification

The most frequently cited theory explaining the motives and benefits of corporate diversification strategy is the resource dependency view (Mehmood, 2015; Marinelli, 2011). Base on the resource dependency postulations, corporate diversification is guided by the availability and capability of resources in an organization (Marinelli, 2011). As a result, the organization diversifies into similar or different industries if it has enough resources and that could be utilize profitably in those industries (Martin & Sayrak, 2003). An improved affiliate postentry performance is linked to the relative size of a business group's new venture affiliate and the level of autonomy inherent in decision-making. Furthermore, when the product market of a new venture affiliate is resource-related to its affiliated business group's main business, this affiliate may benefit from resource relatedness with an improved return on equity (Chen, Tien & Gan, 2018). The issue of both related and unrelated diversification becomes more rational in markets where sale of excess resources and capabilities outside carries significant transaction costs. Therefore, diversification becomes the best way to utilize those resource for the benefit of the organization (Goddard et al., 2008; Subramaniam & Wasiuzzaman, 2018).

By and large, an organization may possess various types of resources (tangible and or intangible) and capabilities that could be used for several beneficial purposes (Fatima, Rehman, & Ali, 2011; Gruber, Heinemann & Brettel, 2010). For instance, in order to improve corporate performance, an organization could make use of its excess cash by lowering the prices, and or buying competitors or suppliers as well as exploiting other tangible resources such as the use of same distribution systems and foreign offices for different business activities operating in different markets (Johnson, Scholes, &

Whittington, 2011). Though, the direction and the level of diversification depends on the package of its available resources and competences, which determines its generalizability (Yaghoubi et al., 2011). If the generalizability of those resources are greater, then the diversification level might be high (Mehmood, 2015). For instance, the excess resources in form of special knowledge drives an organization towards related diversification strategy enabling them to create economies of scope and improve firm performance (Palich et al., 2000).

However, related diversification strategy is better in situations where an organization has surplus resources that could be used for related products and services and or its technology permits manufacturing of related output (Tallman & Li, 1996; Lin & Wu, 2014). On the other hand, corporate organization would prefer conglomerate diversification if excess capabilities and resources are not potentially enough for creating scope of economies among related business activities/operations, but are potentially enough to create internal efficiencies between unrelated business for managing firm performance (Ng, 2007). In evolving economies, group affiliation provides opportunities to certain firms to share several resources such as cash, other tangible resources and valuable information for the purpose of diversifying into related and unrelated areas in order strong competitive advantages in their corresponding markets (Zhao et al., 2013).

Nevertheless, resource dependency theory has been enhanced with new thoughts from various scholars (Mehmood, 2015). The study of Barney (1991, p. 113), improved the classical resource based view of corporations by integrating the idea of sustained competitive advantage if they:

are valuable in terms of exploiting opportunities and neutralizing threats in environment, are rare among its potential and current competitors, are not perfectly imitable and finally do not possess close substitutes.

It could be maintained that the pursuit of corporate diversification strategy solely depends on the corporation's strategic competence defined by its exclusive resources and core capability, and the direction of the strategies (related and or unrelated) rest on the nature of resources and proficiencies it possess. In the event whereby the resources are related with each other, the motive and benefits available to the organization would be inform of synergistic effects and or economies of scope via related diversification. However, if the resources are not related, then the organization would delight in financial economies and or other internal efficiencies through unrelated diversification strategy.

2.6 Governance Mechanisms

Corporate governance is described as the mechanism put in place to harmonize and direct the managers to act in the best interest of the shareholders (Chen, 2014). According to La Porta et al. (2000) corporate governance is the process in which providers of finance to firms guarantee themselves maximum return on their investment. The practices of corporate mechanisms in Malaysian corporate sector can be examined from the directives as contained in the master plan as well as orders from the regulatory bodies. Although, based on the Malaysian code on corporate governance from 2000, 2007, 2012 and the recently introduce 2017 code, the issues are not far fetch from the composition of board, recruitment of new directors, director's remuneration, the use of board committees and their mandates and activities. In summary, corporate governance can be seen as the

relationship between firm's capital suppliers and its management, with the board of directors serving as a link between the two parties.

Corporate governance mechanisms strengthen the fiduciary relationship that existed in the agency contract between the agent (management) and the principals (equity holders, debt holders, suppliers and groups with the stake in the business of the firm) (Goergen & Renneboog, 2016). Black et al. (2015) document that good corporate governance moderates the negative effect of transactions on the firm value and increase the association between firm profitability with that of the industry. Corporate governance mechanisms can either be internal or external. Internal mechanisms comprise the corporate board, board committees, CEO characteristics and other related mechanisms, while external mechanisms consist of external auditors, stock exchange listing requirements, the regulatory frame work of the country, foreign shareholding and enlistment among others.

The following discussions focus on some of the widely used governance mechanisms in academic research and the extent to which these are applied by the Malaysian corporate sector as suggested by the governance reform agenda.

2.6.1 Board Characteristics

Board characteristics refer to the attributes of the boardrooms that influence the process and manner in which the board discharges its responsibilities. These characteristics include board independence, board size, tenure of independent directors, risk management committee among others (Machuga & Teitel, 2009; Wagner, 2011; Zona, 2014).

The board of directors has two main functions which is to monitor and provide resources for the firms they are in, and in theory, it is correlated to firm performance (Hillman & Dalziel, 2003). The board of directors can be regarded as the instrument through which shareholders can affect the behavior of managers, thus aligning the interest of the company and shareholders value (Radford, 2013; Roy, 2016). This brings the need for the boards and shareholders to get more involved in the firm especially towards the decisions on innovation investments (Krishnan & Mohd Amin, 2017). In addition, Honore, Munari, and Potterie (2015) claimed that having effective corporate governance practices, would lead the interests of both the managers and shareholders together which would bring a positive impact on performance. Meanwhile, board monitoring in ensuring the interest of shareholders are protected is an important component of corporate structure (Fama & Jensen, 1983). The board is expected to monitor the management's decision to enable them decide on a more beneficial corporate diversification. Besides, as market control is not active in Malaysia, board governance is expected to serve as an effective governance mechanism (Ishak & Manaf, 2013).

Nevertheless, in Malaysia, like in other East Asian nations, the efficacy of the boards may be limited since they might be controlled by the controlling shareholders. Thus, criticisms have been focused to boards for not always fulfilling their responsibility and fading in their duty to protect shareholders (Johnson et al., 2000; Berger, Imbierowicz & Rauch, 2016). However, the Bursa Malaysia in its listing requirements in 2002 adopted a restriction on the number of directorship for an individual. Under this restriction, a director can only serve a maximum of ten (10) directorship of a public listed companies and not more than

fifteen (15) positions in companies that are not listed. The rationality is to enable them perform their duties more efficiently with less commitments.

2.6.1.1 Board Size

Board size represents the number of persons that sit on the firm board of directors. The board, been a supreme policy formulation body for a firm, decides on the strategies and process that should be adopted by the management (Maigoshi, 2017). It plays a vital role in ensuring proper corporate governance and financial transparency in a firm (Samaha, Khlif & Hussainey, 2015). The results of the studies on the optimal board size remain inconclusive. As a result, some stock markets stipulates a certain range of number that the board size must dwell within (Cheung et al., 2006).

Large board are believed to be effective and beneficial to the firm because as the number of members increases, the firm will also benefit from their diverse and accumulated experiences (Hidalgo, Garcia-Meca & Martinez, 2011). According to Coles, Deniel and Naveen (2008) large boards discharge their monitoring and advising roles more effectively. On the contrary, Sengupta and Zhang (2015) state that effectiveness of board depends on the power of the board relative to that of CEO.

Firms with complex business model need to have a large board to perform better (Coles et al., 2008; Linck et al., 2008). Recent studies document a positive relationship between board size and firm value (Black & Kim, 2012; Upadhyay, Bhargava & Faircloth, 2013). However, this result is more pronounced in large firms (Lappalainen & Niskanen, 2012), because the size of the board in most cases increases as the firm grow bigger (Chen, 2014;

Jameson, prevost & Puthenpuracka, 2014). Michelon and Parbonetti (2012) argue that the number of members that constitute the board plays important role in its decision making process, which may in turns have impact on the firm value. However, many studies established that the impact of board begin to decrease if the board continues to increase after reaching its optimal size (Bozzolan & Beretta, 2015; Choi, Choi, Hogan & Lee, 2013).

Some studies document a negative association between board size and firm value (Mak & Kusnadi, 2005; Guest, 2009). Consequently, Mak and Kusnadi (2005) analyzes the stock value of the firms that uses different corporate governance codes and report that large board size reduces the firm value in both Malaysia and Singapore. Henry (2010) realize that large board is associated with an increase in discretionary expenditure, hence increasing the firm agency cost. Similarly, Troung and Heaney (2013) argue that large board size is detrimental to a firm as it consumes more of the firm scare resources and may lead to free-rider problems among the members. Many government reforms are found to encourage smaller boards (Chen, 2014). Nonetheless, Wahab et al. (2011) find that large boards are more effective in mitigating negative on firm value.

2.6.1.2 Board Independence

The board of directors is a collective body that should act in the best interest of shareholders. The board requires the combination of executive and non-executive directors to pursue the interest of shareholders (Fuzi, Halim & Julizaerma, 2016). The non-executive directors on the board will not be able to exercise their duties effectively, unless they are independent from management and ensure they provide unbiased business judgment. Independent directors are the person entrusted by shareholders to represent them and will

help to reduce agency problems. Further, the MCCG recommend that for the composition of board members to be balanced, it has to consist of independent directors. Independence directors serve as one of the major internal governance mechanisms that reduce the potential opportunistic behaviors of managers in a well disperse organizational setting, or to minimize potential self-dealing by controlling shareholder in a firm with concentrated ownership structure (Adams, Hermalin & Weisbach, 2008; Crespi-Cladera & Pascual-Fuster, 2014).

MCCG (2017) requires independent directors to constitute the majority of the board membership if the chairman of the board happens to be a non-independent director. The presence of adequate number of independent directors on a board has been seen as solution for preserving the interest of all categories of shareholders (Mallin, Mellis & Gala, 2015) and certify that corporate decision are made in a manner that protects the interest of all stakeholders (Lo, Wong & Firth, 2010). Smaller boards with higher proportions of outside directors tend to make decisions about acquisitions, executive compensation and CEO replacement (Hermalin & Weisbach, 2003; Knyazeva, Knyazeva & Masulis, 2013). Hence, the appointment of an independent director on the corporate boards reduces the owner-principal agency problem between controlling shareholder and minority shareholders.

The presence of independent directors is expected to improve general business operations (Maigoshi, 2017). This can be achieved through the expertise that a firm can derive from its outside directors in the areas of business strategy, marketing, finance, operations and more importantly high objectivity in monitoring executive management (Armstrong, Guay & Weber, 2010; Armstrong et al., 2015). Brickley and Zimmerman (2010) opine that

independent directors provide two separate roles to a firm. These roles are advising the executive management as well as monitoring the executive performance.

Independence of directors from the management helps in ensuring objective monitoring, through which advising role can be effectively discharged (Kim, Mauldin & Patro, 2014). It must be noted however that, proper investigation on the genuine independence of outside directors is must, more especially in a market dominated by concentrated ownership. This assessment is necessary because the term outside directors and independent directors are interchangeably used in Anglo-Saxon context to mean independent directors. Nevertheless, the situation is not the same in continental and emerging economies where concentrated ownership is dominant. Under the this situation, outside directors may be nominated by controlling shareholder to supervise management on his behalf, whereas independent directors will be there to protect the interest of minority shareholders or on the free float. So in the event of a conflict of interest between controlling and minority shareholders, the distinction between the two categories is crucial (Fraile & Fradejas, 2014).

Several studies have been carried out in a few countries by examining board independence and firm value (Fuzi, Halim & Julizaerma, 2016). The results from prior studies (Cybinski & Windsor 2013; Liu, Miletkov, Wei & Yang, 2015; Ahmad, Rashid & Gow, 2017) showed mixed relationship between proportions of independent directors and firm value. Although the companies comprised the highest number of independent directors, it would not assure to enhance firm performance. Thus, the existence of independent directors on board should be monitored in order to bring positive shareholder values. Certain studies document a positive relationship between a number of independent directors and firm value (Cybinski

& Windsor 2013; Liu, Miletkov, Wei & Yang, 2015), While other studies reveals negative and insignificance results (Abdul Rahman & Mohamed Ali, 2006; Epps & Ismail, 2009; Fitriya & Locke, 2012; Ahmed Sheikh, Wang & Khan, 2013). The last category documents no association between board independent and firm value (Leung, Richardson & Jaggi, 2013; Ahmad, Rashid & Gow, 2017). Hence, the effect of independent directors on firm value remain debatable.

2.6.1.3 Risk Management Committee

The concept of risk management has become central to corporate governance and is linked to the idea of internal control (Yatim, 2010). Consistent with a risk-based approach, a board that puts in place firm-wide risk management system increases risk awareness within a firm. The increase in awareness and knowledge allows the board for more sound decision making and creates a positive impact on the governance structures and on control environment of the firm (Aebi, Sabato & Schmid, 2012). However, compared to an audit committee, the establishment of a RMC within a firm shows a concerted effort to address risk issues. The RMC will be more proactive in planning a continuous process that identifies, measures, and manages risk in the firm (Hassan, Mohd Saleh, Yatim, & Rahman, 2012). The decision by top management to implement risk management is obtained through a strategic decision-making process where the CEO plays an important role (Ludin, Mohamed & Mohd-Saleh, 2017). The boards of directors that actively participate in risk management are more thorough when reviewing the effectiveness of internal controls (Ong et al., 2016). Therefore, this in turn reduces the likelihood that uncontrolled business risks may cause unexpected losses, reputational damage or strategic setbacks. Further, firms that

are proactive in risk management activities are not only able to detect and prevent frauds but can also enhance their financial reporting quality (Gates, Nicolas, & Walker, 2012).

The risk domain in business is rapidly changing and expanding. Almost anything in business has become a risk factor that will have heady, direct and far reaching effects on businesses (Lai, 2012). An effective risk management practices do not only protect value but also assist in identifying and capitalizing on opportunities to increase firm performance. An operative risk management framework and process helps a company to achieve its performance targets by providing risk information to enable better decisions, both in the setting of company strategy and in daily decision making in which the strategy is executed. The MCCG codifies the principles and best practices of good governance and describes optimal corporate governance mechanisms and internal processes. It requires all public listed companies to institute a formal risk management program to mitigate their business risk. In addition, PLCs were also mandated to report corporate risk management in their annual reports.

The board is ultimately responsible for setting the risk appetite of the company, overseeing its risk management framework and satisfying itself that the framework is appropriate and sufficiently sound in order to respond to evolving business risk (Soltanizadeh et al., 2014). The ability of the board to cultivate a healthy risk culture is integral to the implementation success of its risk management framework. A healthy risk culture among others demonstrate a strong tone from the top and an environment that encourages accountability. In addition, the board should determine the company's level of risk tolerance and actively identify, assess and monitor key business risk in other to safeguard shareholders'

investment and the company's assets. Since the internal controls are imperative for risk management, therefore, the board should be committed to articulating, implementing and reviewing the company's internal control system. Periodic testing of the effectiveness and efficiency of the internal controls procedures must be conducted to ensure that the system is viable and robust. Meanwhile, the board should disclose in the annual report the main features of the company's risk management framework and internal controls system.

Heightened awareness of risk management is largely due to many corporate disasters and unexpected business failures (Walker & Fox, 2002). Consequently, these corporate collapses have alerted investors and corporate governance reform advocates to the importance of sources of risk and uncertainty. The company directors, as a result, have been required to report their internal control mechanisms. For instance, in 2004, the Committee of Sponsoring Organizations of the Treadway Commission (COSO) (2004) issued its Enterprise Risk Management-Integrated Framework that provides a model of the ERM (Enterprise Risk Management) process and defines ERM as:

A process, effected by an entity's board of directors, management and other personnel, applied in strategy setting and across the enterprise, designed to identify potential events that may affect the entity, and manage risk to be within its risk appetite, to provide reasonable assurance regarding the achievement of entity objectives.

The COSO (2004) framework views ERM as an ongoing, systematic process that involves board and senior management in understanding future events that can strategically affect the organization. The primary emphasis is on managing risks affecting the organization's

objectives, including those related to strategy, operations, reporting, and compliance (Yatim, 2010).

Financial crisis and unexpected collapse of many corporations and banks in the US have resulted in relentless consequences, including reduced economic activity, loss of public confidence, and unstable financial system. Many factors may have contributed to these fragilities, however, excessive risk taking is probably one that has also made internal control to be essential (Ng, Chong & Ismail, 2012). Besides, a competitive environment that continues to shape and drive market change, intensifies rivalry among companies and is likely to lead them to undertake even more risks over time. Partly for these reasons, it is imperative to have continuous risk monitoring and assessment in order to uphold corporate accountability (Brown et al., 2009).

The risk management committee (RMC), a unit that used to mean little has now become an important emphasis. Traditionally, risk management activities have been embedded as part of the key functions of an audit committee (Spira & Page, 2003; Sarens & De Beelde, 2006; Fraser & Henry, 2007; Ng, Chong & Ismail, 2012). Depending on the regulatory changes, the scope of an audit committee has been extended to take up risk management and internal control, apart from ensuring integrity and transparency in the financial reporting process. Not only audit directors should be financially literate, the audit committee needs to be familiar with risk management as ways to optimize the checks and balance function (Bank Negara Malaysia (BNM), 2010).

Focusing on the clear fiduciary duties spelled out in various frameworks and guidelines, the audit committee expectedly engages in numerous risk exercises, such as risk

identification, evaluation, management and control. However, the trust placed on the audit committee in protecting shareholders' investments is somehow challenged by a number of corporate failures and scandals, such as in the cases of HIH Insurance, Enron, and WorldCom. The recurrence of business collapses substantially casts doubt about the effectiveness of an audit committee in overseeing and executing risk management program (Bates & Leclerc, 2009; Ng, Chong & Ismail, 2012). The purported multiple roles have been objected by Zaman (2001) and Turley and Zaman (2004) that it is unreasonable to expect an audit committee to carry out high-level review as its members have only limited resources in terms of skills and time. Risk is more than the description defined from a financial perspective; it encompasses politics, economy, regulation, and market (Burton, 2008). Against this background, Bugalla et al. (2012), among others proposed that an audit committee should be independent from an RMC in order to preserve the integrity and protect against fiduciary malfeasance.

The above insights provide two implications – first, it underscores the need to separate duties and responsibilities between an audit committee and an RMC. Second, auditors and RMC members should not be linked in any way to ensure fair assessment of all risk management functions. De Lacy (2005) strongly recommended the setup of an independent RMC given the more complex risk environment. This is similarly supported by Brown et al. (2009) that an audit committee may be unable to oversee both financial and non-financial risks. Moreover, Daly and Bocchino (2006) confirmed that many audit committee members found it uncomfortable to be overburdened with workload in risk oversight. It is believed that a stand-alone RMC is able to strengthen the internal control mechanism (Yatim, 2010).

The increased concern regarding risk management practices has considerably prompted legislative reforms worldwide. In Malaysia, for example, the central bank, BNM made changes in the financial regulatory environment in order to instill corporate governance values in the financial service industry. More specifically, the audit committee has been in principle redefined in terms of roles and responsibilities after the official requirement is announced for the setup of a new committee – the RMC in 2003. From the decomposition of the integrated functions earlier, the audit committee is now focused on maintaining the integrity and transparency of financial reporting process; while the RMC oversees activities conducted by the senior management in key risk areas; in addition to the duty to ensure that insurers have an appropriate risk management process that functions effectively in companies (BNM, 2010). Subsequently, the concept of risk management, corporate governance, and internal control are interlinked (Yatim, 2010) and the RMC turns out to be a key governance mechanism that assists boards and management in managing risks.

RMC is an important element of corporate governance since it provides a means of realizing corporate objectives and monitoring the performance of an agent by a principal (McNutt & Demidenko, 2010). Gates et al. (2012) argued that the RMC monitors the level of risk whilst attempting to maximize returns by advising the board of current risk exposures and future risk strategies, which is in line with MCCG issued by Securities Commission and Bursa Malaysia listing requirements. Likewise, the studies of Zhao, Hwang, and Low (2013) and Culp (2002) considered risk management as consisting of specific efforts that establish a buffer or contingency to absorb economic effects and impose controls that will mitigate the extreme losses of a company. Meanwhile, the MCCG, (2017), mandated the board to determine the company's level of risk tolerance and

actively identify, assess and monitor key business risks to safeguard shareholders' investments and the company's assets.

Studies on the link between the RMC and performance are inconclusive. Cummings and Patel (2009) noted that risk management and financial activities improve the efficiency and consequently the performance of a firm by reducing costs. Contradicting this, Tufano (1996) found little empirical support for risk management practices as a means of maximizing shareholder value. The study of Tufano (1996) discovered that risk management practices of firms, such as hedging to reduce their exposure to risk, are more likely to be related to managerial risk aversion than maximizing shareholder value. In Malaysian context, Yatim (2010) studied the effect of setting up risk management committees in 690 publicly listed companies in Malaysia in 2003. The study discovered a strong relationship between the existence of a risk management committee and board structures, thereby demonstrating a stronger commitment and awareness of the importance of an internal control system. Risk management committees have made a significant contribution to ensuring that risks are mitigated effectively, thereby improving corporate performance. However, the study of Ong et al. (2015) reveals that setting risk management committee made no difference in financial performance. Meanwhile Aebi, Sabato and Schmid (2012) found that there is a collinear relationship between risk management committee and performance, whereas the coefficient on number of meetings of the risk committee is positive and significant.

2.6.1.4 Tenure of Independent Director

Public companies generally do not have specific term limits on director service (Spencer & Stuart, 2011), the rationale being that long-serving outside directors are valued because of their experience and organizational memory. In recent years, some governance experts and market participants have challenged this view. For example, 74% of investors indicate that long director tenure is problematic (ISS 2013-14 Policy Survey). The study of Huang and Hillary (2018, p.8) reveals that:

The Council of Institutional Investors, which manages over US\$3 billion in pension assets, announced a new policy in 2013, calling for boards to evaluate director tenure when assessing director independence, and beginning in the 2014 proxy season, Institutional Shareholder Services (ISS) started to include director tenure in their company governance ratings. ISS views “tenure of more than nine years as excessive by virtue of potentially compromising a director’s independence.”

Outside the US, a growing number of countries have adopted tenure-related guidelines or restrictions on outside directors. With very few exceptions, the “comply and explain” model prevails, and the recommended maximum tenure for a corporate director is between 9 and 12 years. For example, the UK corporate governance code states that a board should explain why a director who has served for more than nine years qualifies as independent. The European Commission recommends that outside directors serve a maximum of three terms, or 12 years. In Hong Kong, an outside director is limited to a 9 years tenure, unless voted otherwise by shareholders. In France, a director is deemed to lose independence after 12 years.

Most importantly, the MCGG (2017) recommends that the tenure of an independent director should not exceed a cumulative term of 9 years. Upon completion of the nine years, an independent director may continue to serve on the board subject to the director's re-designation as a non-independent director. The assessment criteria for independence of directors should also include tenure. Long tenure can impair independence, for this reason, tenure of an independent director is capped at 9 years. The 9 years can either be a consecutive service of 9 years or a cumulative service of 9 years with intervals. An independent director who has served the company for 9 years may, in the interest of the company, continue to serve the company but in the capacity of a non-independent director.

There is a large literature concerning the benefits and costs of directors' tenure (Chan, Liu, & Sun, 2013). Reilly and Caldwell (1981) postulate that directors' organizational commitment increases in tenure. Longer tenure directors may have high job satisfaction and they are less likely to reverse their job acceptance. Thus, extended directors' tenure can enhance the commitment of directors to fulfill their duties and reduce their turnover. In essence, long-tenure directors possess higher commitment and willingness to work better. They also possess greater experience, expertise and reputation which are beneficial to the firm value (Xie, 2014).

On the other hand, long board tenure may lead to entrenchment which reduces the effectiveness of independent directors. Long tenure independent directors are more likely to possess a gradual friendly relationship with the management (Vafeas, 2003). The reason is that their independence is most likely to be compromised as their tenure increase. By a means of controlling shareholders possess the incentives to influence the independent

directors (Anderson, Mansi & Reeb, 2004) and (Securities Commission, 2011a). This particularly applies to firms in emerging markets like Malaysia, as firms in these markets possess high ownership concentration and are mostly family-controlled (Arosa, Iturralde, & Maseda, 2010).

Studies by Bebchuk and Cohen (2005) and Ryan and Wiggins (2004), suggest that management may also use their power to influence the nomination process of directors. Independent directors with strong personal ties with the management are more likely to be re-appointed and survive long term. Long tenure tends to increase a director's knowledge of the firm, allowing shareholders' interests to be better served, these directors might not operate independently because they already possess strong personal ties with the management (Musteen & Datta, 2010; Wilson, 2016). This will also encourage the controlling shareholders to expropriate resources from the firm without significant check and balances from the independent directors at the expense of the minority shareholders (Vafeas, 2003). In addition, long tenure directors are less mobile and less employable. As business operations become more sophisticated and frequently changing, long tenure directors increasingly find it difficult to keep track of the changes in technology, financial dealings, and business strategies as compared with their new counterparts. Besides, the former may lack the talent to deal with new issues (Musteen & Datta, 2010). Huang (2015) shows that board tenure has an inverted U-shaped relation with firm value, and that this curvilinear relation is reflected in performance, financial reporting quality, executive compensation, CEO replacement, corporate strategies and innovation. The results indicate that, for firms with short-tenured boards, the marginal effect of board learning dominates entrenchment effects, whereas for firms that have long-tenured boards, the opposite is true.

Moreover, it can be argued that the entrenchment effects of long board tenure could be higher in family firms compared to non-family firms in the Malaysian capital markets because family controlling shareholders have the incentives to exert more influence on the independent directors due to their interest in managing the firm in their own way to fulfil their private objectives at the expense of minority shareholders (Anderson et al., 2004).

Apart from practical interest, board tenure captures the trade-off between knowledge accumulation and board independence. A board acquires more firm-specific knowledge as board tenure increases, which is associated with an increase in firm value (Huang & Hillary, 2018). However, increased familiarity between the board and management can undermine board independence (Hwang & Kim, 2009; Fracassi & Tate, 2012), which can be associated with a decrease in firm value. Williams and O'Reilly (1998) show that the effect of tenure diversity on team performance is inconsistent across studies, with some positive and some negative results. Although anecdotal evidence suggests that long board tenure is negatively associated with firm performance, empirical evidence on the effect of board tenure on corporate decisions and firm performance remains scarce (Huang & Hillary, 2018).

2.6.2 Audit Committee Characteristics

The listed companies are required to have an audit committee in many countries. This position is based on the fact that existence of audit committee reinforces board's oversight of auditing and accounting practices in firm (Lo et al., 2010). Audit committee members are saddled with the responsibilities for reviewing and monitoring compliance with all financial reporting disclosure requirements (Al-Akra et al., 2010). Brochet and Srinivasan

(2014) argue that audit committee members are required to exhibit a high degree of oversight function on accounting and disclosure issues. Meanwhile Cai, Hiller, Tian and Wu (2015) find that audit committee plays an important role in mitigating agency cost and serve as a substitute for external regulations in an economy with weak legal institutions. It is argued that Audit committee performs its duty effectively when that members are independent, expert and well resourced (Li, Mangena & Pike, 2012).

The roles and powers of an audit committee are provided in the code of corporate governance of the territory in which the firm domicile (Maigoshi, 2017). Mintz (2006) reports that in an American model, for instance, audit committee members are expected to recommend for the appointment, review compensation and independence of an external auditor and serve as intermediary between the board and external auditor. They should review the financial statements of the firm, auditors' reports, authors' inquiries and recommendations as well as management responses to those inquiries.

Assessment of the appropriateness of internal control, major auditing and accounting practices should also form part of their duties. There is much difference between U.S., the UK, and many other common law countries models of audit committee's functions, considering the source of their legal system (Mintz, 2006). MCCG (2000) provide for the mandatory establishment of audit committee in Malaysia. The committee structure, independence and financial expertise have been reinforced by the latest version of the code (MCCG, 2012).

2.6.2.1 Audit Committee Independence

The need for audit committee independence can be linked to the widespread literature on the importance of board independence (Carcello & Neal, 2003). In order to strengthen the independence of audit committees, many countries in the world required that the committee should be chaired by independent directors and independent directors should compose the majority of the committee membership (Black & Kim, 2012; Crespi-Cladera & Pascual-Fuster, 2014).

According to Rainsbury et al. (2008) and Bala, Amran and Shaari (2019) the aim for the establishment of the audit committee is to assist the outside directors of the board to achieve their duties, which are monitoring the management and protecting the interests of shareholders. However, achieving the mentioned task by audit committees depends on their independent members from the management and their qualifications (Aboagye-Otchere et al., 2012; Li et al., 2012; Rochmah & Mohd Ghazali, 2012). Aboagye-Otchere et al. (2012), argued that from the agency theory perspective, the independent members in the committee are important to strengthen the monitoring role of the audit committees, which helps shareholders to monitor the activities of management, and, hence reduce the benefits from withholding information. This is because the independent members in the committee are not related to management, so they will able to enhance the quality and credibility of the reporting, and reduce information asymmetry (Mangena & Pike, 2005).

Empirically, many previous studies have documented that audit independence plays an important role in enhancing the ability of the audit committee to maintain the integrity and quality of the corporate financial reporting process. For example, they find that dependent

members on the audit committee reduces the earnings management (Bedard et al., 2004; Mohd Saleh et al., 2007), increases the accuracy of management earnings forecasts (Ahmad-Zaluki & Wan Hussin, 2009) and is associated with timelier remediation of material weaknesses (Goh, 2009). The results of these studies suggest that audit committee independence plays a significant role in enhancing the effectiveness of the audit committee.

Bedard and Gendron (2010) reviewed the studies on audit committee for the period of 1994 until 2008. The authors reveal that most of the studies document a positive relationship between the audit committee independence and the effectiveness in their financial reporting oversight function. This position is in line with the requirement of many governance codes across the globe. The majority of the members of audit committee are required to be independent (Wan-Hussin, 2009). The MCCG (2012) required that executive director should not be appointed as a member of the audit committee and independent directors should constitute majority of its membership. Abott, Parker and Peters (2004) document an adverse relationship between independence of audit committee and restatement of the financial reports. This highlight the importance of the monitoring role plays by the independent of audit committee members in the financial reporting process. Aldamen et al. (2012) document that audit committee independence improves the firm value.

Independence of audit committee members who have much concern for their reputation and potential legal liability support the external auditor while conducting their assurance services (Lee, Mande & Ortman, 2004). They discharge their monitoring role free from the dictate of management. Therefore, independence of audit committee members is essential in achieving good corporate and financial transparency.

2.6.2.2 Audit Committee Size

The role of the audit committee in most companies is to monitor the integrity of their financial statement as well as the announcements of financial performance. Okeahalam (2004) opined that it is the duty of the audit committee to bring to the notice of the board of directors all issues that require special attention. Whereby, the size of the audit committee is considered to be relevant to the effective discharge of its duties (Al-ebel, 2013). A number of corporate governance reports mandates that audit committees consist of a minimum of four directors (New York Stock Exchange, 2002). It is argued that a larger committee has greater organizational status and authority and a wider knowledge base (Braiotta et al., 2010).

According to the resource dependence theory, a larger audit committee means the members can bring more resources to the firm, such as experience and expertise, which contribute to the audit committee's effectiveness in monitoring management, hence leading to high earnings quality. The Cadbury Report (2000) and the Smith Report (2003) stipulate the number of audit committee members must be at least three; the Sarbanes–Oxley Act (2002) also mandates a minimum of three members in the audit committee. Buchalter and Yokomoto (2003) recommend that audit committees should be composed of three to five members although it is generally based on the firm's size. The MCCG (2012) recommends there should be at least three non-executive directors in the audit committee, a majority of whom should be independent.

The study of Bruynseels, Liesbeth and Eddy (2014) suggest the belief that CEOs often appoint directors from their social networks. In particular, firms whose audit committees

have “friendship” ties to the CEO purchase fewer audit services and engage more in earnings management. Auditors are also less likely to issue going-concern opinions or to report internal control weaknesses when friendship ties are present. On the other hand, social ties formed through “advice networks” do not seem to hamper the quality of audit committee oversight. Social connections between CEOs and audit committee members may reduce audit committee effectiveness (Beasley et al., 2009). However, evidence shows that social ties can sometimes be beneficial for companies that have a high need for advisory services, in case they engage in mergers or acquisitions (Schmidt, 2012).

The existence of an audit committee increases the integrity of firm’s financial disclosures through monitoring financial reporting and audit processes (Christensen et al., 2010). The audit committee provides the greatest level of protection to shareholders as they ensure that the firm complies with mandatory disclosure requirements in providing high quality financial information. Further, an audit committee serves as a corporate mechanism on the board that helps to reduce earnings management practices (Abdul Rahman & Mohamed Ali, 2006; Mohd Saleh, Mohd Iskandar & Mohid Rahmat, 2007).

The strength of the effectiveness of audit committee depends on their adequate resources (DeFond & Francis, 2005; Li et al., 2012; Rochmah & Nazli, 2012). Felo et al. (2003) maintain that a large audit committee is able to identify and address potential problems in the financial reporting process because it has sufficient resources to assume a significant monitoring role. Likewise, Bedard et al. (2004) posit that bigger audit committees are more likely to identify and address possible difficulties in the financial reporting process. As it is expected to provide and ensure effective monitoring through its expertise, strength and

multiplicity of views. This suggests that the size of the audit committee is a critical factor in firms in order to deliver meaningful corporate reporting (Klein, 2002).

According to Anderson et al. (2004), large audit committee provide a greater monitoring function, as there are more members to undertake various tasks involved in monitoring the financial reporting process. The presence of audit members with experience will also reduce financial misreporting and enhance quality monitoring (Hamdan, Sarea & Reyad, 2013). As such, having experienced audit committee members should be a key priority for firms. Also there is need for firms to have an audit committee that is not too small such that there is lack of expert advice and too large such that it has free riders that are prone to follow other members opinion (Al-ebel, 2013).

Empirical studies provide evidence that audit committee size is related to high earnings quality (Hamdan, Sarea & Reyad, 2013; Garcia, Barbadillo & Perez, 2012). Additional evidence from Malaysia shows a significantly positive relationship between audit committee size and earnings quality (Ahmad-Zaluki & Wan-Hussin, 2010; Ismail, Adibah, Dunstan & Zijl, 2009). However, a number of prior studies document an insignificant relationship between audit committee size and earnings quality (Abbott, Parker & Peters, 2004; Xie, Davidson & Dadalt, 2003; Baxter & Cotter, 2009; Adiguzel, 2013; Al-Rassas & Hasnah, 2015).

The study conducted by Al-ebel (2013) investigates whether the monitoring mechanisms influence the IC disclosure in the banking sectors in developing countries, particularly in Gulf Co-operation Council (GCC). The result implies that an increase in the number of directors on the audit committee leads to an increase in the level of IC disclosure, and

supports the argument that when audit committees are well resourced they will be able to monitor the management (DeFond & Francis, 2005). His study argues that larger audit committees play an important role to oversee the information provided in the annual report. Overall, the assertion is consistent with Li et al. (2008) and Li et al. (2012) who find that size of audit committee is positively related to IC disclosure in UK firms. Furthermore, the result is consistent with the findings of Cornett et al. (2008) on earnings management.

Hamdan, Sarea and Reyad (2013) emphasize that there is a positive relationship between audit committee characteristics such as audit committee size, financial experience and audit committee independence, and financial performance of Jordanian firm listed in the Amman Stock Exchange Market. In addition, a similar research conducted by Aldamen et al. (2012) shows that firms with an audit committee that has more experience and financial expertise are more likely to achieve better financial performance compared to other firms. A more recent study conducted by Kipkoech and Rono (2016) revealed that audit committee experience and audit committee size has a significant effect on firm value. Based on the revelations and or findings from prior studies it can be concluded that the association of audit committee size and firm value is still a puzzle.

2.6.3 CEO Characteristics

Chief executive officers (CEOs) possess great power to influence the choice of the strategies and possesses, and therefore, the firm performance (Miller, Minichilli & Corbetta, 2013). It is widely reported that some powerful CEOs use their power to influence the director nomination process to maintain a pliable board (Baldenius, Melumad & Meng, 2014; Hill, Lopez & Reitenga, 2016). Kalyta and Magnan (2008) report that

powerful CEO engages into rent extraction activities in a low quality disclosure environment. Therefore, proper understanding of CEOs characteristics is necessary for explaining corporate performance.

2.6.3.1 CEO Expertise

The CEO possess great power to influence the choice of the strategies and processes, and therefore, the firm performance (Miller, Minichilli & Corbetta, 2013). It is widely reported that some powerful CEOs use their power to influence the director nomination process to maintain a pliable board (Baldenius, Melumad & Meng, 2014).

A CEO is expected to possess some generic skills and talent to deal with varying organizational activities and many external environment such as capital market, media and stakeholders (Maigoshi, 2017). CEO's ability to acquire these expertise has been identified as one of the factors that determine the success of decisions and programs. Custodio, Ferreira and Matos (2013) find that CEOs with general managerial skills accumulated over years of experience receive higher pay package than others. This finding can be justified with the fact that CEOs with financial expertise are financially sophisticated and more likely to manage actively firm's financial policies (Custodio & Metzger, 2013)

According to Haislip and Richardson (2015) CEOs with IT expertise make more accurate estimation and analyst that follow those firms make more accurate earning forecast. They also find that firms with IT experts CEOs announce earning earlier than other firms. In the event of acquisitions and diversification, firms with experienced and expert CEOs in targeted industry records higher abnormal return compared to non-experienced CEO firms

(Custodio & Metzger, 2013). Custodio and Metzger (2013) further demonstrate how CEO expertise affect the market value of firm while taking business strategies decisions. Venture capitalist usually retains the founder CEOs in order to keep their managerial experience and their scientific skills (Dubocage & Galindo, 2013). CEOs talent has been found to influence the firm value (Falato, Kadyrzhanova & Lel, 2014). Additionally, Huang, Li, Meschke and Guthrie (2015) find that firms that focus on the industry in which they possess managerial and financial expertise achieved more significant improvement in performance. The improvement is higher for firms with CEO with much experience in that industry (Maigoshi, 2017). Despite the recorded importance of CEO expertise, previous studies have paid little attention to the effect of CEO expertise on firm value.

2.7 Corporate Governance and Diversification Value

There are several studies that examine the extent to which governance characteristics affects firm value (Knut, 2016). One of the noteworthy studies is by Stulz (1990) in which the author argues that good governance should positively impact a firm's market valuation and performance. Presumably because better governance gives the firm increased access to capital markets and allows it to obtain capital at more favorable terms. This view is also supported through anecdotal evidence coming from the surveys conducted by McKinsey & Company, which show that investors are more than willing to pay a premium for firms employing better governance practices (Davis, Schoorman, & Donaldson, 1997).

However, prior researches conducted on the relationship between corporate governance and firm value were accompanied by mixed findings (Gompers, Ishii, & Metrick, 2003). The first revelation is that, there exist a positive effect of corporate governance on firm

value (Mak & Kusnadi 2005; Krivogorsky 2006; Larcker et al., 2007; Carline et al., 2009; Renders, Gaeremynck & Sercu, 2010; Khan, Tanveer & Malik, 2017). While the second category of studies discovered the existence of a negative correlation between corporate governance and firm value (Hutchinsos & Gul, 2004; Bauer et al., 2004; Giroud & Mueller, 2010). Though, other results generated from the third category revealed that corporate governance has no impact on firm value (Grove et al., 2011; Brenes et al., 2011; Castaner & Kavadis, 2013; Shank, Hill & Stang, 2013; Gupta, Chandrasekhar & Tourani-Rad, 2013). The existence of contradictory relationship between corporate governance and firm performance, is that companies with sound financial performance are more likely to conform to corporate governance norms and standards and implement sound corporate governance system (Surya, 2016). Corporate governance systems vary considerably around the world in terms of their particular mix of mechanisms. Most of the research in the area of corporate governance were conducted in developed economies, as rich data is available for these economies where active market for corporate control exists and the ownership concentration is low. There are good reasons to postulate that the effectiveness of corporate governance might be quite different in developed and emerging markets. Hence, studies on the area of relationship between corporate governance and firm performance in context of emerging nations are essential to get better understanding of the issue.

2.8 Concept of Diversification

Corporations have several alternatives strategies for growth. Ishak (2004) put three strategies, horizontal, vertical and diversification strategies, horizontal, vertical and diversification strategies, in the logical order to be followed by a corporate, as shown in figure 2.1, horizontal growth is the first strategy to consider; this is to keep on expanding

the existing business with its current product range through increased sales volume and geographical extension (Simon, Fischbach & Schoder, 2014). Secondly, after the effect of horizontal growth has been accomplished, the corporation can consider growing vertically within its industry/business base, either forward to its customers or backward to its suppliers. Finally, the corporation choose to diversify. The diversification is labelled as industrial when the corporation diversifies across different lines of industry/business (Denis et al., 2002; Chen & Yu, 2012). The new lines of industry/business that the corporation evolves might be related or unrelated to its current industry/business. Expanding the business geographically, as mentioned in the horizontal strategy, is known as geographical or global diversification, when the corporation diversifies across national boundaries (Ishak, 2004). However, corporate diversification in this thesis refers to industrial diversification only.

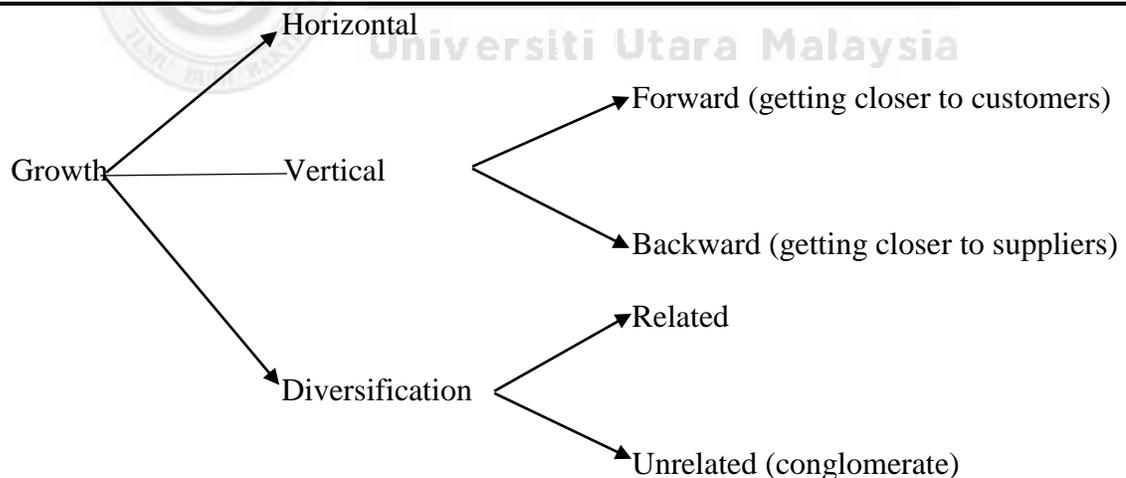


Figure 2.2
Generic Strategies for Growth
(Source: Ishak, 2004, p.53)

Corporate diversification generally is related to the scope of corporate operations or activities. There are two primary avenues for diversification strategies: internal diversifications that rely on development of products or services; and external diversifications that rely on the acquisition of other corporations (Ahuja & Novelli, 2017). Both avenues have advantages and drawbacks. External diversification gives faster growth than internal diversification (Ishak, 2004). However, compared to internal diversification, external diversification may involve paying a premium price for the business (Schommer, Richter & Karna, 2019).

Thus, corporate diversification is regarded as having a managerial motive when managers diversify to benefit their own interest at the expense of corporate owners and or shareholders (Wan & Hoskisson, 2004). Though, managerial motives for diversification have begun to receive greater attention in the financial economics literature. The study of Ishak and Manaf (2013) further revealed that base on the argument that managerial motives are likely to explain corporate diversification, corporations with strong and effective monitoring mechanisms for managers' behavior would diversify less than corporations without such mechanisms in place. However, few researchers associated diversification and governance structures which allowed managers to pursue their personal interest at the expense of the shareholders (Anderson et al., 2004; Ararat et al., 2017). Although, the management assumes the sole responsibility of corporate control, while the board of directors are appointed to represent the shareholders. Hence, the ultimate motive for having a board is to protect the shareholders from "management moral hazard" (Ishak & Manaf, 2013).

Corporate diversification can be partitioned into certain classifications. For instance, there is a national or international (global) diversification (Denis & Sarin, 1997; Castañer & Kavadis, 2013), as well as diversification within the same industry (related) or in an entirely different industry (unrelated) (Erdorf et al., 2013). Nevertheless, for the purpose of this research work, corporate diversification is narrowed down to industrial diversification, although, previous researches study different kinds of corporate diversification strategies and its impact on several firm specific factors, such as excess value (Ishak & Napier, 2006) social and financial performance (Mehmood, 2015; Patrisia & Dastgir, 2016), corporate governance (Kallamu, 2016), firm performance and risk (Kahloul & Hallara, 2010), bankruptcy risk and cost (Singhal & Zhu, 2013) human resource (Neffke & Henning, 2013), and corporate cash holdings (Etemad & Joker, 2016). However, it was suggested by these prior studies that there are several possibilities to investigate a certain type of diversification and its impact on several firm specific factors. Meanwhile, this study examines the impact of diversification strategy on the value of publicly listed firms in Malaysia.

Empirical studies have generally produced mixed results on diversification's overall value effect.' Copeland and Weston (1979) cite several studies that find superior stock price performance by conglomerates over mutual funds in the 1960s and early '70s. Other studies, however, find inferior performance during this period. Ravenscraft and Scherer (1987) argue that the performance of a sample of conglomerates becomes noticeably worse in the 1970s. De (1992) however, finds no cross-sectional correlation between the degree of focus and measures of excess return calculated over the period 1976-85. Other studies addressing the effect of focus on performance also produce mixed results. Chatterjee and

Wernerfelt (1991) review the literature measuring performance with accounting numbers and find that no consensus emerges.

Previous studies generally attribute a comparative penalty to diversification, especially in the 1980s although its magnitude is rarely statistically significant. While these studies examine the buyers of related and unrelated firms, Berger and Ofek (1995) find that increased focus is a significant determinant of seller gains from asset sales. Comment and Jarrell (1994) find a negative relation during 1978-89 between abnormal stock returns and several measures of diversification, including the number of segments reported by management and revenue- and asset-based Herfindahl indexes. Similarly, Lang and Stulz (1994) present evidence of a negative relation between Tobin's q-ratio and these diversification measures

Moreover, the impact of corporate diversification on firm value is a popular and widely discussed subject in literature, and can be divided into three categories. Firstly, corporate diversification in general will lead to a reduction of overall firm value (Aggarwal & Samwick, 2003; Berger & Ofek, 1995; Hoechle et al., 2012). Secondly, firm value increasing effect due to corporate diversification (Choe et al., 2014; Ishak & Napier, 2006; Villalonga, 2004). Thirdly, there is no impact at all (Zahavi & Lavie, 2013). Additionally, others argue that diversification will neither enhance performance nor reduce risk because a corporation may diversify into areas it has less competitive advantage and that the impact of diversification depends on whether it is sectorial, geographical and or industrial diversification (Acharya et al., 2002). Overall, it can be stated that there is still no consensus whether corporate diversification destroys or generates firm value. Hence, this

study analyzes the impact of corporate diversification on firm value using Malaysian public listed company data.

Therefore the research topic concerning the impact of corporate diversification on firm value is most appealing. Recently, a lot of firms are diversified, but does corporate diversification in the end lead to an increase in firm value? There are quite a number a number of studies conducted on the reason why firms diversify and if this diversification increases or decreases firm value. Likewise, there is a discussion concerning the choice of method(s) to measure the impact of corporate diversification on firm value, whether they are appropriate or biased (Rudolph & Schwetzler, 2014). Meanwhile, it is highly essential for corporate managers to know if a certain diversification strategy is worthy to pursue in terms of an increase in firm value.

2.9 Corporate Diversification Value

The growing popularity of business diversification has aroused great interest among academics and practitioners concerning firms' motivation to embark on diversification strategy as well as the failure or success of such a strategy in creating value for firms (Mehmood, 2015). The implications of this corporate strategy for value creation have sparked discussions in both finance and strategic management (Bhatia & Thakur, 2018). The diversification value linkage constitutes a prolific area for research, since maximizing long-term firm market value has been placed at the top of objectives which guide firms' activities (Kallamu, 2016)

The debate about diversification being a value-creating or a value-destroying strategy has given rise to a closely related line of research based on the existence of a premium or a discount of the diversification value (Custodio, 2014). In prior literatures, several theories on the benefits and costs associated with diversification have been developed (Mehmood, 2015). The first benefit of diversification, which gives rise to diversification premium, involves the creation of internal capital markets in which divisions with high cash flows but limited investment opportunities can finance divisions with low cash flows but promising investment opportunities (Shen, Au & Yi, 2018). Second, diversification may benefit firms by a coinsurance effect derived from combining businesses with imperfectly correlated earnings (Espinosa-Méndez, Jara-Bertín & Maquieira, 2018). This effect reduces firms' unsystematic risk and thus increases value (Faccio, Marchica & Mura, 2011). Third, diversification creates a tax advantage by allowing the losses of some segments to be offset by the profits of others (Mehmood & Hilman, 2017). In addition, the resource-based theory suggests that diversified companies may share resources among divisions and thus benefit from economies of scope (Bryant & Davis, 2012). Finally, diversified firms can create and exploit market power advantages by using some anticompetitive tools that are unavailable to focused companies, such as predatory pricing, collusion, or reciprocal buying (Patrisia & Dastgir, 2016).

On the other hand, there are costs to corporate diversification, which give rise to diversification discount. The first cost of diversification is related to agency theory, which considers diversification as an activity that managers undertake for their own benefit, at the expense of shareholders (Rudolph & Schwetzler, 2014). Diversification may benefit managers because of the power and prestige associated with managing a larger firm

(Jensen, 2010), since managerial compensation is related to firm size (Almudena, 2016), or for the reason that diversification reduces the risk of managers' undiversified personal portfolios (Brick, Palmon & Wald, 2018).

Another cost of diversification is related to overinvestment problem and internal capital markets (Mehmood, 2015). If managers have a general tendency to overinvest, then access to an internal market for capital in a diversified firm simply provides a greater opportunity to overinvest in negative NPV projects (Jensen, 2010). Similarly, diversified firms can provide cross subsidies to unprofitable lines of business (Ojo, 2009). Corporate diversification might be value destroying for some firms due to inefficient allocation of capital among different segments, which may result from information asymmetry between central managers and divisional managers (Custodio, 2014).

There is also evidence which indicates that multi-segment firms trade at a discount relative to a portfolio of single-segment firms (Hoechle et al., 2012; Custodio, 2014). Berger and Ofek (1995) provide empirical evidence supporting that multi-segment firms invest inefficiently and, consequently, trade at a discount in relation to similar constructed portfolios of single-segment firms. Custodio (2014) explain the value destruction by means of overinvestment and cross-subsidization of multi-segment firms. Rudolph and Schwetzler (2014) find that divisional resources do not appear to be directed to segments with the most favorable investment opportunities. From another perspective, De Andrés, Fuente and Velasco (2017) argue that investors prefer focused firms since it is more convenient for them to achieve the desired level of risk diversification with pure-play firms.

Consequently, diversified firms would trade at a discount because of lower transparency and lower liquidity.

In one of the first papers on diversification discount, Wernerfelt and Montgomery (1988) estimated the effects of diversification, industry structure, and market share in determining the performance of US firms. They found that diversification has a negative impact on firm value, as measured by Tobin's q . In finance literature, the seminar papers on diversification discount are Lang and Stulz (1994) and Berger and Ofek (1995). Preceding work on conglomerates had compared ex post performance of diversified firms to the performance of single-segment firms. By contrast, they decomposed diversified firms into their segments and then valued these segments using benchmark companies. Lang and Stulz (1994) found that diversified firms trade at lower Tobin's q than comparable single-segment firms over the period 1978-1990.

Berger and Ofek (1995) were able to confirm the results of Lang and Stulz (1994) for the period 1986-1991. In their paper, the authors used assets, sales and earnings multipliers instead of Tobin's q . Both the authors related their empirical findings to overinvestment and cross-subsidization theories. Later on, Servaes (1996) studied data for US firms covering the period from 1961 to 1976 and documented a large diversification discount during the 1960s, but this discount declined to zero during the 1970s. The author argued that agency problems which manifest themselves as higher insider ownership may explain the higher discount in diversified firms. Denis et al. (1997) and Anderson et al. (2000) were also able to confirm evidence of a value loss from diversification for US firms.

A second group of studies questioned the previous evidence that diversification destroys value. The findings of these studies suggest that diversification, in itself, does not destroy value. But, they argue that factors different from diversification are responsible for the documented diversification discount. Once these factors are controlled for, the diversification discount may decrease or disappear.

Within this strand of literature, Duchin (2010) argued that, several studies fail to control for endogeneity. Using instrumental variables to control for exogenous characteristics that affect the decision to diversify, the author found that the diversification discount either decreases or disappears entirely. Similarly, Villalonga (2004) argued that conglomerates are different prior to beginning their diversification program, and caused the diversification discount to disappear using econometric methods of causal inference. In another study, Hann, Ogneva and Ozbas (2013) offered the risk reduction efforts by diversified firms as an explanation for diversification discount. The authors found that measures of firm value based on book values of debt instead of market values systematically undervalue diversified firms relative to single-segment firms. Using a contingent claim framework and controlling for risk effects, the authors found that diversification does not destroy value, but rather results in a wealth transfer from shareholders to bondholders.

Hoechle et al. (2012) found that diversification discount decreases or even disappears using a dynamic panel generalized method of moments (GMM) estimator to control for endogeneity and controlling for corporate governance. The studies in the second group do not contest the finding that diversified firms sell at a discount. Instead, they argue that the discount is not due to diversification itself but is as a result of a given firm selling at a

discount prior to diversifying. There is also a third group of studies which question the existence of the diversification discount phenomenon itself and argue that diversified firms may trade at a premium (Dastidar, 2009). Differences in these and previous results are attributed to the use of sample selection bias, different measures, time periods, or databases (Erdorf et al., 2011).

One issue emphasized within this strand of literature is a possible sample selection bias (Erdorf et al., 2011). The studies documenting a diversification discount implicitly assume that single segment firms are a valid benchmark for valuing divisions of conglomerates. If this assumption is invalid the documented discount may decrease or disappear. For instance, Hyland and Diltz (2002) found positive abnormal returns for diversifying acquisitions for the 1980s and 1990s. In a study using detailed data on control chains of 710 European commercial banks, Saghi-Zedek (2016) found that when banks have no controlling shareholder or have only family and state shareholders activity diversification yields diseconomies. However, as long as the control chain involves banking institutions, institutional investors, industrial companies or any other combination of these shareholder categories, banks benefit from diversification economies: they display higher profitability, lower earnings volatility and lower default risk.

In their study, Miller (2006) and Hashai (2015) created a measure of technological diversity based on citation-weighted patents and the interplay between adjustment costs, coordination costs and within-industry diversification; found a positive relationship between diversification and market-based measures of performance. In another study, Whited (2001) and Matvos and Seru (2014) caused the discount to disappear by employing

a measurement-error consistent estimator of Tobin's q . Villalonga (2004) hypothesized that the diversification discount could be due to the inappropriateness of the segment data from Compustat used in most previous studies. She used business information tracking Series data and documented a diversification premium. He (2009) argued the diversification discount documented in earlier studies can be an artifact of the pre-1997 data. Using post-1997 data, the author documented a significant diversification premium. Ishak and Napier (2006) document no evidence to support the argument that diversification reduces the value of companies. However, their finding is consistent with the argument that high control rights of controlling owner might encourage expropriation of minority interests through corporate diversification strategies. Thus, corporate diversification is perceived as a mixed blessing strategy.

Non-US studies show that diversification discount exists in some countries whereas others have a premium. Based on coinsurance arguments, for US firms over the period from 1998 to 2006, Hann et al. (2013) state that diversified firms can lower the cost of capital and thus can improve diversification value. Using a sample of Australian listed firms over the period 2004 to 2008, Choe et al. (2014) find that diversified firms enhance firm value more than undiversified firms, and this positive effect is accelerated when firms' managers receive incentives such as stock or stock options. In studying the impact of corporate diversification on diversification value during a recession period, Volkov and Smith (2014) find a significant increase in the value of diversified firms. In another study, Lins and Servaes (1999) found that a discount existed in Japan and UK, whereas no discount was found in Germany. Their results showed that corporate governance structures play a role in diversification discount. Lins and Servaes (2002) documented a diversification discount

in seven emerging markets for the year 1995, and offered the agency theory explanation for their findings.

Stowe and Xing (2006) study the growth opportunities of diversified firms and find that, on average, diversified firms have fewer growth opportunities than do single-segment firms and that the excess value of firms becomes significantly lower after diversification. Using annual data from non-banking firms listed on the Tunis stock exchange, Boubaker et al. (2008) find strong evidence of a discount value on diversified firms: that is, corporate diversification decreases firm value. Singh et al. (2007) analyze the relationship between corporate diversification and performance for Indian firms and find that diversified firms perform significantly worse than focused firms. They also find a significant negative relationship between the degree of diversification and firm performance and conclude that this is a result of the cost inefficiencies of diversified firms. Bae et al. (2011) investigate the relationship between corporate diversification and firm value in Korea and find that while unrelated corporate diversification decreases diversification value, related corporate diversification has no effect. They state that this negative effect is exacerbated if the firm is affiliated to a large business group. Using a sample of 607 listed companies on the Bombay stock exchange from 1999 to 2000, George and Kabir (2012) indicate a negative effect of corporate diversification on firm value.

In a more recent study by Ellouze and Mnasri (2019) on the effect of business group diversification on firms' value, examine whether this effect is particularly relevant for financially constrained firms. They assess this relationship using a unique hand-collected database of 67 Tunisian non-financial firms affiliated with business groups during the

period of 1998–2016. Their study provide evidence that there is a quadratic U-shaped relationship between group diversification and firms' value. They suggest that group diversification enhances affiliated firms' value only if it exceeds a certain threshold. Their results also show that a high level of business group diversification is particularly beneficial for firms that suffer financial constraints.

Bhatia and Thakur (2018) study the causal relationship between extent of diversification and performance among Indian companies. The results report that the association between diversification and performance turn strongly significant and positive after controlling the issue of endogeneity. The study finds a strong two-way relationship between extent of diversification and firm performance. As indicated by the results, the extent of diversification is positively related to performance, thereby implying that diversified firms experience a significant diversification premium. The study also demonstrates a positive relation of performance and total diversification indicating that good performance leads to greater diversification.

However, the rest of the empirical research in emerging countries offers a different picture, studies in Malaysia (Ishak & Napier, 2006; Mehmood, 2015), China (Li & Wong, 2003; Yiu et al., 2005), India (Khanna & Palepu, 2000a; Ramaswamy et al., 2004), South Korea (Lee et al., 2008), and Chile (Khanna & Palepu, 2000b) report that most conglomerates enjoy higher value than focused firms. Mishra and Akbar (2007) also found that diversification through group affiliation is beneficial for Indian companies and that these benefits are more pronounced in case of related diversification. The success of diversified

business groups is mostly explained by a better access to capital markets and closer relationships with bureaucracy (Khanna & Palepu, 2000).

In a comparative study, Fauver et al. (2003) have used databases from 35 countries. The authors documented a significant diversification discount among high-income countries. By contrast, for lower income countries, they found that there is either no diversification discount or a diversification premium. The authors offered two theoretical explanations for their empirical findings: better access to funds through internal capital firms may be more valuable lower income countries. Also, diversified firms may be able to attract better employees and better influence the regulatory process in developing countries. As it becomes clear from the preceding discussion, the majority of empirical evidence on diversification was based on US firms. Diversification could have two opposite effects for developing country firms: internal capital markets may lead to higher value for diversified companies due to greater market imperfections in these economies. On the contrary, greater information asymmetry in developing country firms may lead to a diversification discount through agency costs (Lins & Servaes, 2002).

To sum up, there are both benefits and costs to diversification, with the average net effect being an empirical question. The answer to this question depends on the time period, geographic location, data, and statistical methods used for estimation (Kuppuswamy & Villalonga, 2010). Most of the empirical studies on the value effects of corporate diversification have been conducted for developed economies and the majority of these developed country studies, especially the earlier ones, provided mixed evidence on the

value effect of diversification. Hence, studies on the area of corporate diversification value in the context of emerging nations are essential to get better understanding of the issue.

2.10 Motives for Diversification

Many arguments have been made about why firms diversify. Ojo (2009) claimed that there are many possible motives behind diversification. Montgomery (1994) and Ojo (2009) examines the three perspectives that synthesize a number of individual points. Two of these, the market-power view and the resource-view, are consistent with profit maximization, but only the latter is consistent with the efficient use of resources. The other agency view is managerial in nature, and is consistent with neither profit maximization nor efficiency.

2.10.1 Synergistic Motives

The first and obvious motive is shown in cases where synergy exists when individual units are operated as a single organization. Synergy occurs when the sum of all businesses together equals more than the sum separately (Hitt, Ireland & Hoskisson, 2012; Sirmon et al., 2011). Amit and Livnat (1988) argued that diversification into related businesses may augment the market power of the diversified company which in turn may help the company enhance its long-term strategic position. Additionally, synergy may be created if operations of the individual units complement one another, so there are benefits from offering consumers a complete line of products. The size and reputation of such a firm might deter entry to the industry.

2.10.2 Financial Motive

This motive is based on the fundamental premise of portfolio theory that “one should not put all one’s eggs in one basket”. It may also be argued that a firm should diversify and not depend on a single operation. As shown in finance theory, whenever the cash flows of the individual units are not perfectly correlated, the total risk, as measured by variability of consolidated cash flows, is reduced by diversification (Amit & Livnat, 1988; Gomez-Mejia, Makri, & Kintana, 2010).

2.10.3 Market Power Motive

Under this motive, diversified firms have conglomerate power which makes them thrive on their diversity (Purkayastha, Manolova & Edelman, 2012; Knecht, 2013). In his own view, Gribbin (1976) says a firm will not have conglomerate power if it does not hold significant positions in a number of markets. This power then propels the firm to enter new markets through predatory strategies supported by its position, resources and strength in its current market (Mulwa, Tarus & Kosgei, 2015). Montgomery (1994) explains three possible sources for the market power view:

- ❖ Cross-subsidization, a firm may use its excess profit from one business to enter in another, and hence give this new venture an advantage.
- ❖ Mutual forbearance, companies can meet on another market to compete less severely.
- ❖ Reciprocal buying, large and diverse firms can also buy reciprocally in other markets to seal competition from smaller competitors.

Lindstrom (2005) highlights the anti-competitive actions often associated with motives for diversification. The diversified companies are able to exploit, extend, or defend their power by strategies and tactics. In conclusion, the market power motive is not thought of as to increase efficiency, companies diversify to gain market power, and thereby earn profits.

2.10.4 The Agency Motive

There are number of motives behind diversification from an agency perspective that will not benefit the principal. The reason for this is the separation between the owner and manager, where the manager does not own any equity (Ojo, 2009). This is in agreement with Sambharya's (2000) and Colombo, Piva and Rossi-Lamastra (2014) motive for diversification that it may reflect top management aspirations and goals. Four main reasons for managers to diversify the company are:

- ❖ Empire building, the managers diversify in order to create their own empire (Montgomery, 1994)
- ❖ Managerial entrenchment, managers will diversify into markets or products in a way that increases the demand for their skills and abilities (Shleifer & Vishny, 1989)
- ❖ Risk reduction, managers try to reduce their employment risk by diversifying into different markets and products and thereby make the organization less dependent on a single market or product. The basis of portfolio theory that states that a firm should not put all her egg in one basket (Amit & Livnat, 1988)
- ❖ Free cash flow theory, instead of paying stake owners the managers spend the excess cash flow on acquisitions (Jensen, 2010). The reason for this is that in the

beginning of the firms life cycle there are lot of profitable opportunities for reinvestments, however, when the firm becomes mature these opportunities become more scarce and hence the cash flow from earlier innovations are being used for opportunistic diversification.

2.10.5 The Resource Motive

The resource view argues that rent-seeking firms diversify in response to excess capacity in productive factors, here called resources (Montgomery, 1994). These include factors the firm has purchased in the market, services the firm has created from those factors, and special knowledge the firm has accumulated through time (Tarun & Yishay, 2007). According to Penrose (1959) the attainment of a "state of rest" (equilibrium position) is precluded by three significant obstacles: "those arising from the familiar difficulties posed by the indivisibility of resources; those arising from the fact that the same resources can be used differently under different circumstances, and in particular, in a 'specialized' manner; and those arising because in the ordinary processes of operation and expansion new productive services are continually being created" In this view, so long as expansion provides a way of more profitably employing its underused resources, a firm has an incentive to expand.

Teece (1982) and Makri, Hitt and Lane (2010) pointed out that the economies of scope Penrose described have no direct implications for the breadth of the firm unless their external transfer is subject to market failure. That is, if a firm's unused resources can be efficiently sold in the market, the rationale for diversification evaporates. It is reasonable to expect, however, that market failures do exist in the sale of many of these assets,

particularly as one moves from physical assets the firm has purchased to the services and knowledge it has created itself. Many of a firm's skills and much of its knowledge are deeply imbedded in the routines of the firm (Kim, Lee & Cho, 2016). The transfer of these systemic resources may require the transfer of organizational as well as individual knowledge (Makri, Hitt & Lane, 2010). Further, there are well-known contracting problems involved in the sale of intangible assets (Wan et al., 2011).

The resource view suggests that a firm's level of profit and breadth of diversification are a function of its resource stock. Chen and Yu (2012) noted that a firm's resources differ in specificity. They argue that more specific resources, such as productive skills in biotechnology, may only efficiently be applied in a small number of industries, but may yield higher marginal returns due to their specificity. In contrast, less specific factors, such as standard-issue milling machines, may transfer further and provide the basis for a widely diversified firm, but support lower rents because they are in wider supply. This has important implications for predictions made by the resource view. Because firms are different, they will have different optimal levels of diversification. For a firm with less specific resources, profits may be maximized at a relatively high level of diversification even though a firm with more specific resources could obtain absolutely higher profits with less diversification.

Conventional wisdom suggests that the bigger the company the more resources it controls, hence it should perform above average in an industry (Ojo, 2009). This wisdom is the resource-based motive which states that bundled resources and capabilities that are aggregated over time also underpin a company's competitive advantage (Hill, Jones &

Schilling, 2014). When a firm has underused resources that can be profitably employed, it also has an incentive to expand. Furthermore, diversification is driven by the need to use these excess resources (Ojo, 2009). In order to grow the firm needs to specialize and the profit or resources from the successful growth will be underused and eventually used to growth by diversification.

2.11 Theoretical Basis of Diversification

The main motivation to diversify is the rational starting point for us to understand the performance of the diversified firms. Academic scholars are more kin in this question, which is also related to the basic economics topics; the nature of firm and the efficient boundaries of a firm (Mehmood, 2015). There four main two main important lines of theories underpinning this study: The agency theory, resource dependency theory, transaction cost economics (TCE) and market power view. Just like the conflicting evidences at the empirical, the theoretical studies also provide inconsistent arguments on the relationship between corporate diversification and firm performance. A brief discussion on the theories are presented below.

2.11.1 Transaction Cost Economics (TCE) and Internal Capital Market

TCE and concept of internal capital market provide powerful arguments for the drive and benefits of product diversification strategy. TCE (Williamson, 1971) implies that managers have to choose between external markets and internal organizational hierarchies for structuring and conducting business transactions and they need to carefully compare the relative costs of conducting transactions inside the organization against those through external market (Liu & Hsu, 2011). Providing the main idea of TCE, Coase (1937) argued

that a firm would continue diversification until a point was reached where the costs of conducting additional transaction inside the firm were levelled to costs of conducting the same transaction with outer market or they become equal to costs of conducting the same transaction with another firm.

Under TCE assumptions, it could be argued that a diversified organization might be more efficient compared to a single segment firm and could make better investment decisions because it has its own internal capital market (Berger & Ofek, 1995; Kuppuswamy & Villalonga, 2010; Lins & Servaes, 1999) with the help of which, it could make successful allocation of resources across different businesses to improve its performance (Datta, 1991; Galván et al., 2007). Varanasi (2005) added that diversification could lead to creation of interaction economies through simultaneous supply of inputs and processes across different units. Diversified organization could also gain performance benefits by combining businesses which have different flow of earnings (Berger & Ofek, 1995) or lowering variation in year by year cash inflows (Bhide, 1993). Diversification through backward and forward integration might lead to better performance through savings in production and transaction costs because in industries where the organization is working might be engaged in customer-supplier relationships (Fukui & Ushijima, 2006).

However, the benefits of TCE and internal capital market efficiency could be conditional and might not apply to all multi-business organizations. In unrelatedly diversified organization, sharing of knowledge, implementing internal control mechanisms and gaining cooperation among businesses could be difficult compared to those following related diversification strategy and therefore, in unrelated ones, governance costs and

transaction costs could be greater (Abdullah, 2009), which could erode internal market advantages. In related diversifiers, excessive levels of diversification beyond optimal point could increase the marginal cost of product diversification causing erosion of internal market efficiency (Park, 2010). Similarly, if an organization has an inefficient internal capital market, its costs will increase if changing industry conditions offer tremendous growth opportunities in one segment and in that case it will be optimal for diversified organizations to refocus (Campa & Kedia, 2002; Mackey, Barney & Dotson, 2017). Additionally, internal capital markets might also be disadvantageous in related as well as unrelated diversifiers due to their slow reaction time, high overhead costs, and continuous cross subsidization of badly performing businesses (Berger & Ofek, 1995).

Moreover, diversification benefits on the basis of TCE and internal capital market efficiency are interpretable in light of different institutional contexts in various countries as well as conditions in the external environment (Kuppuswamy & Villalonga, 2010). After the World War II, the pace of conglomerate diversification increased because of the view that corporate headquarters were more efficient in allocating resources and managing various strategic business units as compared to external capital markets (Gupta et al., 2007; Nippa et al., 2011). But diversification gave up its popularity during 1980's and early 1990's because of development of external capital markets in developed economies, particularly in U.S. (Gupta et al., 2013).

In well developed economies, there are efficient product, labour, and capital markets which provide incentives to organizations for external market transactions, and therefore in developed economies, conglomerates might not be successful because external market

transaction costs are lower compared to internalization (Mishra & Akbar, 2007a; Nippa et al., 2011). Therefore, organizations prefer external market transactions in conditions when external markets perform well, because in that case they might have lower transaction costs (Nippa et al., 2011). However, in developing countries, internal capital market could provide greater rewards as external markets are not well developed (Fan et al., 2008; Arnoldi & Muratova, 2019) and in these conditions diversified group structure might be more beneficial and diversification strategy (related or unrelated) might result in better performance (Mishra & Akbar, 2007).

The arguments regarding TCE and internal capital market gained support during 2008-2009 crisis. For instance, in a research on American firms, Kuppuswamy and Villalonga (2010) reported that value of conglomerate diversification increased during the crisis due to ‘more-money’ and ‘smarter-money’ effect attached with internal capital markets. Similarly, in a study of banking industry of nine countries, Elsas, Hackethal, and Holzhäuser (2010) reported evidence against conglomerate discount during sub-prime crisis starting in 2007. Hence, in agreement with Park (2010), it could be added that diversification levels need to be managed carefully keeping in view the external conditions and institutional context.

Summarizing the above discussion, it can be said that TCE and internal market efficiency arguments provide support for the benefits of related and unrelated diversification strategies in perspective of emerging economies such as Malaysia. Thus, the perspectives laid by TCE and internal capital market have strong relevance to this study as the present

study has been conducted in Malaysian context where it provided a test of TCE and internal market efficiency arguments.

2.11.2 Market Power View

Market power advantages could also provide strong motives to strategic decision makers for pursuing product diversification strategy as highly diversified organizations can enjoy their market power in several ways in contrast to focused firms (Benito-Osorio et al., 2012). For example, in contrast to a focused firm, a diversified organization with a variety of products and services possesses the opportunity to cross-subsidize a weak product using profits attained from a strong product, hence providing itself a better competitive advantage for the weak product (Johnson et al., 2008).

Further, a diversified organization could use tactic of reciprocal buying and selling by developing favorable reciprocal arrangements with organizations which are its suppliers and customers at the same time (George, 2007). To illustrate, an arrangement could be established where a company's supplier could be purchasing certain outputs from one of the business unit being acquired by the company and this diversification would result into multiple relationships with other Organisations (buyers or suppliers) providing it greater market power and high performance (George, 2007; Goddard, McKillop & Wilson, 2008).

Moreover, diversified organizations might use income generated through one market in another market for the purpose of predatory pricing i.e. price cutting (Goddard et al., 2008; Klier, Welge & Harrigan, 2009). Using this, a diversified organization could create entry barriers for new entrants, and push existing rivals out of the market, thus bringing itself a

strong strategic position as well as safer business environment in concerned industries (Benito-Osorio et al., 2012). Another advantage of market power could be possible in form of ‘mutual forbearance’, according to which multiproduct organizations would compete less severely amongst themselves when they are competing in number of geographic segments (Mehmood & Hilman, 2015). However, according to Berry-Stölzle, Hoyt and Wende (2013), this situation might also apply to single product firms. Overall, the views expressed herein support the argument that related or unrelated diversification strategy is beneficial for an organization as it provides increased market power.

Based on the above discussions of the underpinning theories of corporate diversification, it could be suggested that there could be various motives, benefits and or consequences for pursuing diversification strategies. Related diversifiers might perform better as compared to single segment firms as per they achieve increased market power and resource management benefits. In addition, diversified firms performed better in emerging economies as they enjoy the benefit of lower internal transaction costs and efficient internal markets (Mehmood, 2015).

2.12 Diversification Strategies

Base on several prior studies, industrial or product diversification might be classified into three practices, such as the related and unrelated diversification (Zahavi & Lavie, 2013; Hashai, 2015; Oh, Sohl & Rugman, 2015; Patrisia & Dastgir, 2016; Su & Tsang, 2015). Related diversification strategy deals with the expansion of business in a similar product or in the same business line which is also known as backward/ forward integration (Chen & Yu, 2012). While unrelated diversification refers to a strategy associated with the

extension of company's operation into a different line of business which has a diverse input- output formation or has a limited common resources (Castañer & Kavadis, 2013). In addition, Patrisia and Dastgir (2016) revealed that a company which adopts related diversification strategy, deals with related products and services, and or participates in the same industry. Meanwhile, Collins and Montgomery (2008) believe that related diversification involves building shareholders value by capturing cross business strategic fits, use of common sales force to persuade customers, use of same brand names and joint delivery, advertising related products together as well as the combination of resources to create new competitive strengths and capabilities.

Eukeria and Favourate (2014) noted and revealed that in most cases companies that go for unrelated diversification always venture into new business by acquiring an established company rather than setting a new subsidiary. The basis for this strategy is that, growth by acquisition translates into enhanced shareholder value faster coupled with quicker payback period. Similarly, a company with unrelated diversification strategy has different products and services and or participates in a different industry and market. Moreover, total diversification is a summary of both related and unrelated diversification strategies (Oh et al., 2015). Therefore, it can be deduce from the above insinuation that diversification strategies are used to expand the firm's operations by adding markets, products, services, stages and or production to the existing business.

2.12.1 Related Diversification Strategy

This strategy deals with the company's expansion into new line of product and markets which is still within the existing strategic business capability (Mehmood & Hilman, 2015).

As such companies company's new line of business activities are related with the existing undertakings (Lahovnik, 2011) and the businesses are similar to each other in terms of input and operational requests. In relation to the specific motivations for diversification, most corporations decide to diversify into related businesses in order to achieve economies of scope (Almudena, 2016). Therefore, this strategy seems to be the result of a profit seeking attitude to thrive and survive in the business context due to economies of scope which can lead to a reduction in total costs and an increase in firm profitability and performance (Galan & Sanchez-Bueno, 2009). In particular, related diversification enable a firm to share and transfer critical success factors across different businesses leading to efficiencies in resource allocation and ultimately to cost advantages (Wan et al., 2011). Moreover, firms can also reduce total costs by exploiting interrelationships between businesses based on technical and managerial skills and functional specialization (Zhou, 2011).

2.12.2 Unrelated Diversification Strategy

Unrelated or conglomerates diversification deals with company's expansion beyond its current strategic capability (Brenes, Montoya & Ciravegna, 2014) whereby its new business and or subsidiaries have little or no relatedness with the old or existing businesses (Mehmood & Hilman, 2013). The unrelated diversification strategies are mostly motivated by empire building desire by some managers (Almudena, 2016). Although unrelated diversification may involve some unique benefits resulting from financial synergies, such as risk reduction and coinsurance, this strategy tends to be an easy alternative for rapidly increasing firm size (Colpan & Hikino, 2005; Griffin, 2013). On the other hand, corporate growth is more beneficial to top managers whose pay, status and job security tend to be

determined more by the firm size rather than its profitability (Aggarwal & Samwick, 2003; Laeven & Levine, 2007). Consequently, due to the nature of firms size in developing nations as compared to the developed countries, the pursuit of managerial self-interest via empire building seems to be the most influential motive for their conglomerates strategies (Almudena, 2016). Therefore, the unrelated diversification strategies for these nations may be considered a strategy for enhancing firm size and benefits for top managers, subject to a minimum profit constraint (Benito-Osorio et al., 2012).

2.12.4 Related versus Unrelated Diversification Strategies

Based on the review of relevant literatures, it was concluded that much like the vagueness about diversification and performance relationship (Marinelli, 2011; Nippa et al., 2011) the issues concerning the superiority of related and or unrelated diversification strategies is as well unresolved (Lahovnik, 2011; Mehmood & Hilman, 2013). The study of Rumelt (1974) pioneered the research of comparing related against unrelated diversifiers and stated that related strategy performed better than the unrelated strategy. His findings were later on supported by the work of Christensen and Montgomery (1981). Afterwards, Michel and Shaked (1984) revealed conflicting results by stating that unrelated diversifiers performed better than the related strategy based on market measures of performance. Subsequently, several attempts were made to compare both strategies on numerous performance measures.

2.12.5 Superiority of Related against Unrelated Diversification Strategy

Quite a number of scholars that concluded in favor of related diversification strategy outperformed unrelated strategies (Galván et al., 2007; Mehmood, 2015; Mishra & Akbar,

2007). Based on the analysis of their studies, it was evident that they used several approaches to measure diversification strategies and also arrived at different conclusion. For instance, some studies used Rumelt (1974) categorical scheme for measuring diversification (Christensen & Montgomery, 1981) others engaged simple categorical measures (Berger & Ofek, 1995; Mishra & Akbar, 2007) while others employed the entropy measurement (Palepu, 1985; Mehmood & Hilman, 2017).

Likewise, the studies comparing related against unrelated diversification strategies adopt different measures of firm performance. For instance, some researchers used the accounting indicators (Eukeria & Favourate, 2014; Markides & Williamson, 2007) while others utilized market based performance ratios (Galván et al., 2007; Mishra & Akbar, 2007; Ooi et al., 2014) certain other research work employed a combination of both accounting and market ratios (Berger, & Ofek, 1995; Mehmood & Haim, 2015). Though mixed results were reported by some studies that used multiple indicators of performance (Christensen & Montgomery, 1981). Additionally, some studies recommended the need for including multiple performance measures in diversification studies for the sake of acquiring better knowledge on the subject matter (Mehmood, 2015). Mehmood further suggest that the use different performance measures obviously revealed the robustness of the findings that related diversification strategy perform better than unrelated strategy on various performance measures.

However, there are still distinction among those studies with regards to the sample sizes, time frame and context of the research. With respect to the sample size, the study of Palepu (1985) relied on 30 firms, while Berger and Ofek (1995) conducted their study on a large

sample of 3659 firms. Likewise Ramanujam and Varadarajan (1989) used their sample from multiple sectors sample from multiple sectors however Palepu's (1985) relied on sample of firms from food industry alone, whereas Mehmood (2015) focus on listed diversified PLCs. Besides, there are also substantial proofs based on the superiority of related diversification over unrelated strategy in multiple context as those had diversified contexts, such as the Eurozone countries (Galván et al., 2007) Asia (Mishra & Akbar, 2007) and or Fortune companies (Rumelt, 1982). In summary, the general conclusion of these researches supports the superiority of related diversification over unrelated strategy.

2.12.6 Superiority of Unrelated Strategy against Related Diversification Strategy

Considerable studies revealed that unrelated diversification strategy performed better as compared to related strategy (Dubofsky, 1987; Marinelli, 2011). As argued earlier, the results of Michel and Shaked (1984), regarding the superiority of unrelated diversification against the related strategy contradicts the outcome of Rumelt's results (1974, 1982) which is in support of related superiority. Afterwards, their results later reaffirmed by the work of Dubofsky, (1987) who used same sample as of Michel and Shaked (1984). However, differentiated his study by introducing additional performance indicator, which is return on asset.

Accordingly, the work of Lahovnik (2011) and Ooi et al. (2014), revealed that unrelated diversification strategy performed better than the related strategy. In a similar rein Marinelli (2011) conducted his study in same direction and also reported result in favor of unrelated diversification superiority, While the study of Meijer (2015) was also recently documented with additional support to the superiority of unrelated strategy. Although, the

studies in support of the superiority of unrelated strategy were different from one another with regards to their methodology (Mehmood, 2015), their general conclusion supported the superiority of unrelated diversification strategy over the related one. However, it could be concluded that there is still no definite consensus on the relative superiority of one diversification strategy over another.

2.13 Diversification and firm Value

In recent times, interest has ascended in the investigation into the diversification practice in the developing countries and or emerging markets, when evolving economies, such as that of Malaysia are increasingly contributing significantly in the global economy (Mehmood, 2015). While few studies have been conducted on the impact of corporate diversification on firm performance has been previously studied (Dimitrov, Jain, & Tice, 2006; Elif , 2015; Almudena, 2016). Evidence from the emerging markets on the causal effects of diversification strategies on firms value is still lacking and or contradicting just as that from advanced or developed countries (Mehmood & Hilman, 2015).

Certain researchers concurred on the lack of consensus on the precise nature of the relationship between diversification strategy and firm performance. As some studies have shown that diversification is a value increasing strategies (Choe et al., 2014; Elif, 2015; Ishak & Napier, 2006; Villalonga, 2004) while other studies revealed that diversification has a value reducing effects on performance (Aggarwal & Samwick, 2003; Berger & Ofek, 1995; Hoechle et al., 2012). Additionally, others argue that diversification will neither enhance nor reduce firm performance (Ammann & Hoechle, 2012; Becerra & Santala, 2004; Eukeria & Favourate, 2014; Mehmood, 2015; Zahavi & Lavie, 2013). Santalo and

Becerra (2008) who were on the same wave length with the work of Stowe and Xing (2006, p.787) generally, concluded that:

(a) The empirical evidence is inconclusive (b) models perspectives and results differ based on the disciplinary perspective chosen by the researcher (c) the relationship between diversification and performance is complex and is affected by intervening and contingent variables such as related versus unrelated diversification, as well as the mode of diversification (i.e. moderately or highly diversified).

However, the work of Daud et al. (2009) revealed that studies in this area tends to have provided conflicting and or inconclusive results due to the nature of inconsistent data, different performance measures and indicators as well as intervening variables and different time frame. In addition, Mackey and Barney (2006) contend that the conflicting outcomes are not far fetch from the issue of different measures of diversification, various measures of profitability and different timeframe. The study of Andreou and Louca (2010) further emphasize that the contradiction is relatively methodological and partially theoretical. Although many efforts have been put into investigating the relationship between diversification and firm performance, but the empirical evidences turn out to be a “puzzle” (Li, 2007). Empirical studies alone may not help to solve this puzzle, for diversification and performance relationship is neither a pure statistical phenomenon nor an issue of whether the benefits exceed the cost (Li & Rwegasira, 2008). In order to have a better apprehension on how to deal with this puzzle, most importantly, is to understand the diversification strategy used by firms and the degree of diversification attained. In

which without investigating into the strategy and degree of diversification, getting the right answer will be difficult.

2.14 Corporate Diversification in Malaysia

Before 1997, corporations in Malaysia were able to expand and diversify because of the availability of easy credits at a relatively low cost to borrowers (Fatimah, 2001). This diversification has been established by researchers such as Ahmad et al. (2003), who found that 53% of the companies in their sample reported multiple segments in 1995, implying that they involved in several industries. Study of Claessens et al. (1998), based on nine East Asian countries found that 70% of Malaysian companies reported multiple segments in their annual reports which was second to 72% for Singapore. Ishak and Napier (2006) also reported significant diversification at around 55% for Malaysian PLCs in 2000. Similarly, recent study of Doaei et al. (2014) also shows considerable level of international diversification for Malaysian companies. Meanwhile, scholars have reported that these levels of extensive diversification from Malaysian PLCs might have resulted in misallocation of investments in less profitable and more risky business segments (Claessens et al., 1998).

Amidst, importance of carefully selecting the level of geographic diversification for the companies (Duru & Reeb, 2002) has as well been highlighted by scholars (Hilman, 2015). It is noted before that companies usually might go for product or geographic diversification for getting benefits of internal capital market. But, past research on product/geographic diversification-performance relationship conducted for Asian countries, including Malaysia had inconclusive results. In this regard, certain researches revealed that

diversification strategy negatively impacted performance or it was not beneficial strategy in certain ways (Lins & Servaes, 2002; Tongli, Ping & Chiu, 2005) which is contrary to arguments of internal market efficiency. During the period before 1997, some corporations became ambitiously involved in construction and property development (Fatima, 2001). Initially, diversification had some economic and strategic value. Within a short time, however, these corporations became diversified beyond their core competencies and capabilities (Hilman, 2015). It is believed that diversification into unrelated areas in which the corporations had no expertise was one of the causes of the financial crisis in Malaysia (Ishak, 2004).

During the occurrence of Asian financial crisis in mid of 1997, Malaysian economy had been marking high growth for a decade for over 8% per annum, lowering rates of unemployment, escalating pressures on wage rates, and overinvestment in properties and infrastructure facilities (Asid, 2010). Malaysia is rapidly shifting itself into knowledge-based, service-focused economy in number of leading industry sectors and market segments (Muhammad et al., 2010). Formerly a struggling economy, Malaysia now is an “Asian Tiger” with an inspiring and impressive growth rate in manufacturing as well as service sectors for the previous few decades (Naqshbandi & Idris, 2012).

As regards features of Malaysian corporate sector, Malaysia has been characterized by presence of high percentage of product and geographically diversified companies (Ahmad et al., 2003; Doaei et al., 2014). Particularly, among private companies, diversified business groups are the most prominent corporate houses operating across a diversified choice of segments across various sectors such as manufacturing, industrial products, trading and

services, construction, finance, property investment and property development, and plantation.

Most importantly, given the fact that there is a huge percentage of diversified PLCs in Malaysia, though few studies are available (Hilman, 2015) on the impact of product diversification on performance, nonetheless research into interaction impacts of the two strategies on corporate performance for Malaysian PLCs is extremely limited (Doaei et al., 2014; Yaghoubi et al., 2011) which indicates an important research gap. Hence, a research into this area is warranted.

2.15 Moderating Variables used in Prior Studies

Based on the analysis made from past researches, it revealed that even though research efforts regarding virtual effects of related and unrelated diversification strategies on firm performance enhanced our general understanding on the subject matter, yet the conclusions were mixed. This suggests that the relationship between corporate diversification strategies and performance is not simple but rather it is contingent on certain factors. Consequently, in order to address such issue, past researches used certain moderating variables in the relationships between corporate diversification strategies and performance (Choe et al., 2014; Li, 2007; Ravichandran et al., 2009; Almudena, 2016).

For instance, the study of Christensen and Montgomery (1981) enhanced on the general conclusion offered by Rumelt (1974) which revealed that market structure and characteristics played moderating role in diversification and performance relationship. Meanwhile the study of Markides and Williamson (2007) discover that the relationship

between related diversification and firm performance depend upon organizational structures that could allow the transfer and allocation of strategic assets across various divisions or segments. Likewise, the study conducted by Hill et al. (1992) revealed that related diversifiers performed better if their organizational structure and control system were designed to facilitate cooperation, whereas, unrelated diversifiers could also gain optimal performance if the control system and organizational structure were designed to facilitate competition.

Additionally, a study conducted by Ravichandran et al. (2009) on the moderating effect of information technology on both related and unrelated diversification strategies and corporate performance relationship. The result show that there is a moderating effect by information technology spending in the relationship between related diversification and firm performance. The work of Mehmood (2015) considered corporate parenting role as a crucial issue related to corporate diversification strategies. In order to reconcile the inconsistencies concerning diversification and performance relationship by focusing on the moderating effect of corporate parenting roles on the relationship. The study revealed that synergy manager positively moderates relationship between related diversification strategy and Tobin's Q, and price to book value. Parental developer positively moderates relationship between related diversification strategy and all financial measures of corporate performance. Portfolio manager positively moderates relationship between unrelated diversification strategy and return on assets, and return on equity. However, on the basis of the prevailed discussions, it could be resolved that better insights could be gained by incorporating an important variable suggested by Li (2007) which is "managers' wealth maximization".

Li (2007) asserts that while the diversification is driven by manager's wealth maximization pursuing, there would be two potential influences on the firm performance considering both the consistence and divergence between manager's discretion and shareholder's welfares. On one hand, manager's wealth maximization is consistent with shareholders' value, therefore the influence will be positive. Due to the complex and non-routine characteristics of the management, especially the top managers', as well as the long lasting effect of the decision-making and other intervening variables between managers behavior and corporation performance, normally firm will design the incentive system or the compensation system on the base of firm performance instead of behavior elements. Thus, diversification to achieve manager's wealth maximization will serve the shareholders' at the same time. On the other hand, some personal benefits such as prestige, power and perquisites can be derived from managing a more diversified firm. These are the benefit that shareholders don't enjoy from the operation. Therefore, the managers might diversify the firm at the expense of shareholders.

Ueng and Wells (2001) provide empirical evidences that the combination of lower incentive ratio and more diversified acquisition instead of the focused acquisition produces the lowest return. Thus, their study supports the assumption that manager of an acquiring firm may pursue personal wealth maximization rather than shareholder wealth maximization. Even managers who pursue their wealth maximization might knowingly undertake value-decreasing investment. Aggarwal and Samwick (2003) argue that diversification discount should be ascribed to the private benefit explanation. They document that diversification, incentives, and firm performance are equilibrium responses to changes in the level of private benefits that managers derive from diversification.

Consequently, although there is some extent of consistence between manager's wealth maximization and shareholder's welfares, empirical studies strongly suggest that manager's wealth maximization would induce negative diversification value (Li, 2007). Therefore, this study moderates the relationship between corporate diversification strategies and firm performance by manager's wealth maximization.

2.15.1 Managers' Wealth Maximization

On the basis of utility maximization premises, many researchers contends that corporate diversification facilitates managers' wealth maximization goal instead of shareholders' value maximization (Li & Rwegasira, 2008). Managers' wealth maximization functions comprises of both monetary rewards, such as salary, and bonus options as well as non-pecuniary benefits associated with managing larger corporation, for example, prestige, power, and perquisites such as company cars, offices among others. Specifically, the non-monetary rewards are the benefits diversification provides to managers and shareholders do not enjoy Li (2007). Diversification obviously provides managers an avenue for increased compensation and may also serve as a motive for increased diversification in order to maximize their monetary gain (Hoskisson & Hitt, 2011).

Whether the company grows internally and or externally, there exist a relationship between the level of managers' wealth and firm size, as reported by a number of prior studies, such as (Choe et al., 2014; Hoskisson & Hitt, 2011; Li, 2007; Ueng & Wells, 2001). Particularly, a more recent study by Choe et al. (2014) which investigate the relationship between manager incentive structure and diversification, comes up with the conclusion that managers with lower ratio of incentives (market value of shares) is not substantially

relative to his total compensation, may decide to undertake more diversified acquisition than managers with a higher incentive, in order to maximize their returns (wealth).

Another empirical study that was earlier conducted by Rose and Shepard (1997) investigated the relationship between CEO compensation and corporate diversification over a period of 1985 – 1990, revealed that the monetary compensation of CEO of a firm with two line of businesses gets an average of 13% additional salary and bonuses than that with similar sized firm from a focused (un-diversified) firm. This implies that wealth maximization is a factor that accounts for more diversification. The study of Berry et al. (2006) further supported the findings of Rose and Shepard (1997) by stating that CEOs in diversified firms are paid more than those in focused companies.

While corporate diversification is driven by managers' wealth maximization pursuing, there would be two potential influences on the firm performance considering both the consistence and divergence between the manager's discretion and that of shareholder's welfares. As argued that manager's wealth maximization is consistent with increase in shareholder's value, therefore, the influence might be positive. Thus, diversification to achieve manager's wealth maximization will in turn serve the shareholders at the same time. The managers may diversify at the expense of the shareholders, since there are certain personal benefits (such as prestige, power, and perquisite) they enjoy as a result of diversification (Li, 2007)

Correspondingly, the study of Ueng and Wells (2001) further support the assumption that manager of an acquiring company may pursue personal wealth maximization interest, rather than the aim to increase shareholders wealth. As a result, this might make the

managers to deliberately undertake a value decreasing investment in order to satisfy their personal interest at the detriment of the shareholders. In addition, the study of Aggarwal and Samwick (2003) is also consistent with the work of Ueng and Wells, whereby contends that diversification discount should be ascribed to personal benefit explanation. Their study revealed that diversification, wealth maximization and firm performance are equilibrium responses to changes in the level of private benefits managers derived from corporate diversification. Moreover, there are certain degree of correspondence between manager's wealth maximization shareholder's value, empirical studies strongly suggests that manager's wealth maximization motive might either induce positive or negative diversification value (Li & Rwegasira, 2008).

Agency theory provides a different perspective on strategic scope decisions, proposing that managerial decisions regarding the scope of the firm may be less than optimal due to conflicts of interest between the agents (managers) and the principals (shareholders). Proponents argue that the separation of ownership (embodied within the "principals") and management (embodied within "agents") can result in the expropriation of firm value (agency costs) by said agents (Adner & Zemsky, 2016). Corporate diversification can work to the benefit of managers at the expense of shareholders in a number of ways. Managerial compensation, for example, increases with the firm's size and strategic scope (i.e., higher levels of diversification), though such higher diversification levels may not necessarily result in improved profitability (Jensen, 2010). Furthermore, the risk of total firm failure is reduced in a diversified firm, and thus managerial employment risk is subsequently reduced. Scope decisions made under circumstances such as these impose agency costs on the firm, in that diversification activities driven by such motives serve managerial financial

self-interests (higher compensation and job security), while providing no financial benefit to shareholders (Choe et al., 2014).

Then there is the concept of “managerial entrenchment” (Wiersema & Beck, 2017). Managers may specifically direct diversification activities into businesses that increase the firm’s dependence on said managers’ particular skills, thus increasing the firm’s dependence on them as specific individuals. Personal position, again, is enhanced at the expense of shareholders.

A final example is in the agency cost of free cash flows (Jensen, 2010). Cash flow in excess of the amount sufficient to fund all positive net present value opportunities presents a temptation to managers. Arguably, that excess cash flow should be returned to shareholders, to do with as they see fit. Such a course of action would, however, represent a dilution of managerial power by reducing the amount of resources under managerial control. Diversification into a line of business with a negative net present value, while detrimental to shareholders, presents managers with a means through which to retain control over said resources.

The essence of the agency theory argument is that there are many ways in which managers can benefit from a strategy of diversification (even if shareholders do not). Managerial opportunism and the existence of free cash flows are thus seen as significant motivating factors underlying decisions to pursue corporate diversification. Appropriate corporate governance structures, through which managers are effectively monitored, as well as incentivized compensation schemes, through which managers’ interests are aligned with those of shareholders, can reduce such agency costs.

The external capital market, with the threat of hostile takeovers of poorly performing firms, can provide a further deterrent to value-destroying diversification strategies. The takeover constraint, the risk that managers face of the company being acquired, can limit the extent that managers will pursue value-destroying strategies. Evidence suggests that such market pressures have led to refocusing strategies through which such conflicts of interest have been mitigated and performance improved (Wiersema & Beck, 2017).

2.16 Stakeholder Theory

Stakeholder theory has been utilized in both management and accounting literature, ever since it was conceptualized by Freeman in 1984 (Yusoff et al., 2006; Yusoff & Darus, 2012). The term stakeholder refers to any group or individual who has a legitimate claim on the firm. A firm has many stakeholders, some of them are: stockholders, employees, suppliers, managers, customers among others. Each of these groups can be seen as supplying the firm with critical resources, and in exchange each expects its interests to be satisfied (Crane & Livesey, 2017). A separation is made between internal and external stakeholders. According to Van Puyvelde et al. (2012), managers are internal stakeholders and customers or suppliers are examples of external stakeholders. Friedman (1970) argue that stakeholders theory have more responsibility for creating economic value to maximize shareholder wealth.

However, Jensen (2002) and Scott (2015) contends that firms should pay attention to all their constituencies, the theory is unassailable. Taken this far, stakeholder theory is completely consistent with value maximization, which implies that managers must pay attention to all constituencies that can affect the firm. But, there is more to the stakeholder

story than this. Any theory of action must tell the actors, in this case managers and boards of directors, how to choose among multiple competing and inconsistent constituent interests. Customers want low prices, high quality, and expensive service, among others. Employees want high wages, high quality working conditions, and fringe benefits including vacations, medical benefits, pensions, and the rest. Suppliers of capital want low risk and high returns. Communities want high charitable contributions, social expenditures by firms to benefit the community at large, stable employment, increased investment, and so on. And so it goes with every conceivable constituency. Obviously any decision criterion and the objective function is at the core of any decision criterion must specify how to make the tradeoffs between these often conflicting and inconsistent demands.

Every stakeholder of a firm creates value for the company. Since management are considered to be stakeholders of a firm, the manager is also included in this consideration. Thus according to this theory the manager is also affected by the outcomes of the firm. A positive firm performance will eventually make his position stronger. This will make the probability of him being fired smaller. Besides, this can also be applied to the topic regarding managers' wealth maximization and firm performance. Thomsen and Conyon (2012) describe that the view of corporate expenditure of managers' change when they buy or receive company's stock. Thus changing the compensation structure or setting appropriate incentives for the managers can give positive results to the firm.

Jensen (2010) opine that the main contender to value maximization is stakeholder theory, which argues that managers should attempt to balance the interests of all corporate stakeholders, including not only financial claimants, but employees, customers,

communities, and governmental officials. By refusing to specify how to make the necessary tradeoffs among these competing interests, the advocates of stakeholder theory leave managers with a theory that makes it impossible for them to make purposeful decisions. With no clear way to keep score, stakeholder theory effectively makes managers unaccountable for their actions (which helps explain the theory's popularity among many managers).

However, if value creation is the overarching corporate goal, the process of creating value involves much more than simply holding up value maximization as the organizational objective. As a statement of corporate purpose or vision, value maximization is not likely to tap into the energy and enthusiasm of employees and managers. Thus, in addition to setting up value maximization as the corporate scorecard, top management must provide a corporate vision, strategy, and tactics that will unite all the firm's constituencies in its efforts to compete and add value for investors.

While manager control becomes a normal sense, Amihud and Lev (1981) and Gomez-Mejia et al. (2010) do find evidences that manager-controlled firms engage in more conglomerate acquisitions than owner-controlled firms, and the operations of manager-controlled firms are more diversified than those of owner-controlled firms. This empirical study implies that diversification, as a strategic decision is largely driven by the managerial considerations, or under the management control, instead of the owners, or other stakeholders. In the case of highly dispersed ownership structure, it is rational for the manager to be the decision-maker, not only in the strategic decision-making such as

diversification but also the daily management operations (Li, 2007; Phung & Mishra, 2016).

From diversification's point of view, it matches the strategic control from managers instead of the financial control from important shareholders, thus in the sense of practice, diversification favors manager control. Strategic control means business evaluation is based on subjective criteria and the operational aspects of the strategies. Thanks to short of firm-specific knowledge, shareholders as outsiders couldn't fully understand organizational operations, so that they focus more on the financial control, which relies on objective criteria for evaluation, such as return on investment, Return on Assets and so on. For this approach to work, the firm's business units must be independent enough to disclose the relevant information. In fact, diversification leads firm's businesses into much more complex, and the accounting report in most situations is less informative. As a consequence, financial control by shareholders could not be efficient in case of diversification, and could not be effective when it might diminish creativity and innovativeness in the organization (Almudena, 2016).

Needless to say how complex the reality is, and there are wide latitude between purely managers' control and purely owners' control. Somehow, as discussed above, it is still reasonable to say that the decision to diversify is largely under the manager's control in the large public traded corporations. The rationality is based on the efficiency consideration.

2.17 Literature Gap

A number of previous studies investigated the role of governance mechanisms in resolving conflicts of interest between shareholders and managers as well as in improving performance (Alabede & Muff, 2016; Darko et al., 2016; Guney et al., 2007). However, the results from prior studies produce mixed findings. The indecisive nature of the literature as it relates to whether there is any relationship existing between corporate governance and firm performance is been functioned as a call for this research work.

In addition, corporate governance mechanisms have been extensively studied by prior researchers in developed countries (Brick & Chidambaran, 2010; Radford, 2013; Roy, 2016). There is still need to further examine the relationship between corporate governance mechanisms (for example, board size, tenure of independent directors, board independence, risk management committee, audit size, and independence, and CEO expertise) and firm performance of public listed companies in the Malaysian context. However, the existence of inconsistent relationship between corporate governance and firm value, will not be far-fetched from the use of different proxies, methodologies, samples, and techniques to gauge the effects of corporate governance on firm value. Most of the research in the area of corporate governance were conducted in developed economies, as rich data is available for these economies where active market for corporate control exists (Knut, 2016). There are good reasons to postulate that the effectiveness of corporate governance might be quite different in developed and emerging markets (Saravanan, 2012). Hence, studies on the area of relationship between corporate governance and firm value in the context of emerging nation like Malaysia is essential to get better understanding of the issue, since sufficient study in this area is still needed.

Issue concerning the impact of corporate diversification on firm value is most appealing. Recently, a lot of firms are diversified (for instance, there are about 490 diversified firms in Malaysia), but does corporate diversification in the end lead to an increase in firm value? There are quite a number of studies conducted on the reason why firms diversify and if this diversification increases or decreases firm value. Likewise, there is a discussion concerning the choice of method(s) to measure the impact of corporate diversification on firm value, whether they are appropriate or biased (Rudolph & Schwetzler, 2014). Meanwhile, it is highly essential for corporate managers to know if a certain diversification strategy is worthy to pursue in terms of an increase in firm value. This scenario compels the requisite to study the effects of corporate diversification strategies and their relationship with firm performance of listed Malaysian PLCs. Therefore, given its research objectives, this study may contribute to more and/ or better understanding of the relevant phenomenon concerning Malaysian companies, while filling the contextual gap on the research topic.

In addition, to the best of the researcher's knowledge, there was no any previous study that documented the extent of corporate diversification strategies and its effects on diversification value, measured with excess value (sales, assets & earnings multipliers). This study is the first of its kind that fills in this literature gap by documenting the level of corporate diversification strategies and its effects on diversification value. Furthermore, previous studies have concentrated on the use of financial indicators to measure firm value (Berger & Ofek, 1995). Certain few efforts have been put in place to measure corporate diversification value with excess value (see for example Berger & Ofek, 1995; Ishak, 2004; Ishak & Napier, 2006; Stowe & Xing, 2008).

This study has contributed to the recent trend in corporate diversification strategies studies by using all the three industrial multipliers (sales, assets & earnings) to measure excess value. Examining diversified firm with excess value has several advantages over the accounting measures (Berger & Ofek, 1993). Using the industry multiplier approach on individual business segments has several advantages over other methods. For instance, studies that assess value effects using accounting and market based methods provide only limited opportunities to examine the potential sources of gains or losses from diversification. The industry multiplier approach not only provides a direct estimate of the excess value associated with diversification, but also allows further investigation at the segment level of the sources of any overall value effect (Stowe & Xing, 2006).

From the theoretical perspective, the empirical findings on how paramount the corporate governance and diversification strategies are to be structured to boost corporate performance and serve the interest of shareholders using diverse theoretical views remain inconclusive (Combs, Perryman, & Donahue, 2007; Daily, 2002). Correspondingly, prior researchers proclaim that one theory alone cannot adequately explain the interaction between corporate governance mechanisms, diversification and firm performance (Arosa et al., 2010; Jackling & Johl, 2009; Mehmood, 2015), thus integrating multiple theories may provide better understanding of dynamism of corporate governance. Hence, this justifies the use of agency theory, resource dependency theory, transaction cost economic view, market power view and stakeholder theory as a guide to this research work in order to fill the research gap.

There is limited research that investigate managers' wealth maximization role as moderator in diversification - performance relationship. Nevertheless, Fama and Jensen (1983) address the importance of managerial incentives to investment decision. While Jensen and Murphy (1990) argue that the sensitivity of managers' pay for performance is an important factor of corporate governance. However, managers may have myopic behavior either to partake over and or under investment activities, if the managerial compensation plan places much emphasis on short-term stock return and little or no attention on future performance (Chen & Chen, 2012). Aggarwal and Samwick (2003) further revealed that diversification discount should be ascribed to the private/personal benefit description. They also discovered that diversification, incentives and firm performance are equilibrium responses to changes in the level of personal benefits the managers derive from diversification. In a similar vein, the work of Anderson and Fraser (2000) find that diversified firms with higher CEO equity-based pay, usually have higher excess value of firms. Therefore, we expect that the investment efficiency is likely to be affected by the sensitivity of managers' wealth maximization and the performance of diversified firms. However, this study aims to further validate the aforementioned claimed by investigating the effects of diversification strategies (related & unrelated) on firm value by taking wealth maximization role as the moderator in the relationship.

2.18 Chapter Summary

This chapter was devoted to the review literature on relevant theories and past studies. It started by providing detail on Malaysian corporate sectors along with number of PLCs, governing bodies and Bursa Malaysian markets. Then it presented basic conceptualization and definition of corporate governance structures and diversification strategies along with

its types. This was followed by explanation on the underpinning theories of both corporate governance and diversification. A critical analysis was also presented on past researches conducted on exploring the effects of corporate board and diversification strategies on firm performance as well as detailed discussion on examining the relative superiority of either related on unrelated diversification strategy and vice versa.



CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

Based on the earlier chapters, this chapter discusses the theoretical framework that supports the variables used in the study. In particular, the chapter highlights and links the agency theory, resource dependence theory, transaction cost economic theory, market power theory and stakeholders theory with the variables used in the study. Based on the foregoing theories, the supportive literature hypotheses were developed accordingly. The chapter also discuss the control variables of the study, as well as the research design. The section that follows then concentrates on the operationalization and variable measurement, population and sampling, method of data collection and analysis as well as the model specification. Finally, the chapter closes with the summary of the chapter.

3.2 Theoretical Framework

The theoretical framework proposed for this research is presented in Figure 3.1. This framework is based on research questions and research objectives earlier provided in chapter one. The framework indicates that two of the objectives of this research is to test the effect of corporate board and diversification strategies on firm diversification value (using excess value). Whereas the figure also shows that another objective of this study is to test moderating effect of Manager's wealth maximization between diversification strategies and diversification value. In modern companies, there is a separation between managers and owners. Consequently, the managers have better access to a company's private information than the owners.

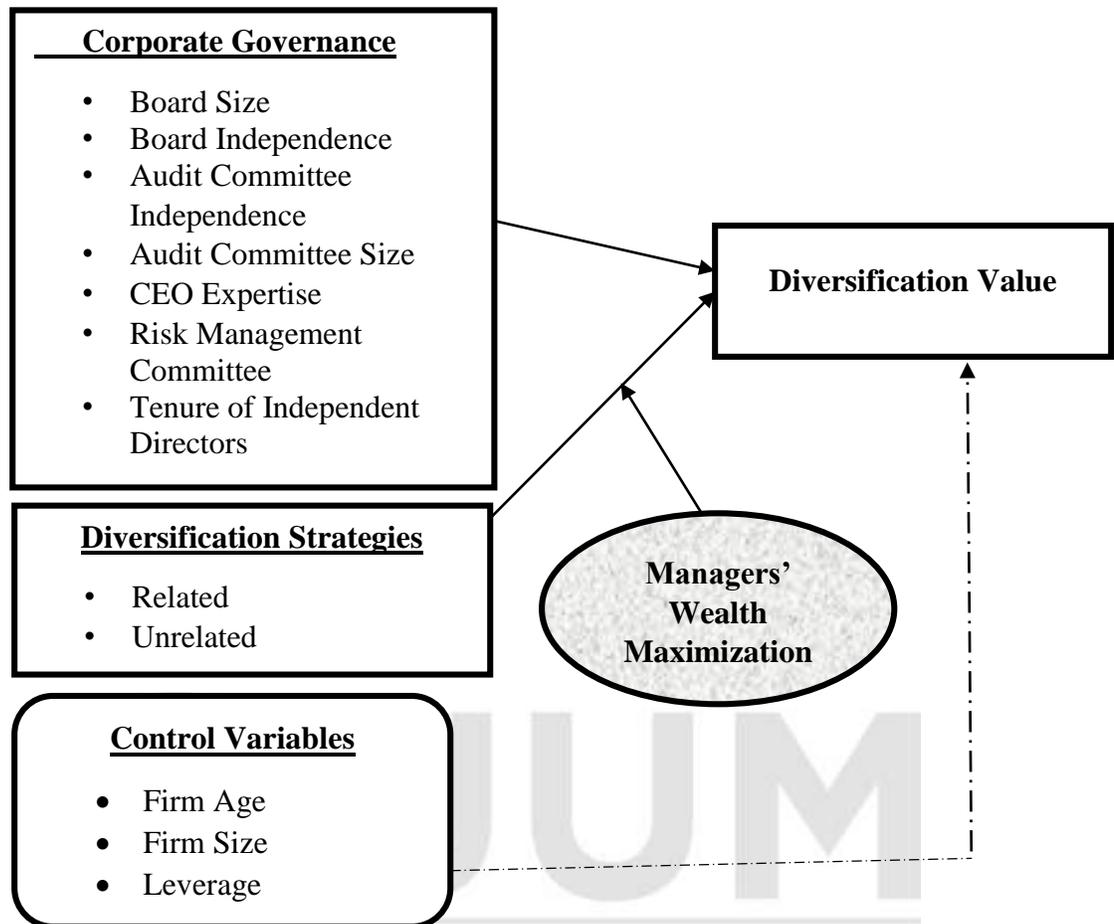


Figure 3.1 Theoretical Framework

The basic view apprehended by agency theorist on corporate governance is that, in any given circumstance, the controlling managers may not perform to maximize shareholders returns in contrast to their personal interest, unless appropriate governance mechanisms are put in place in order to protect the shareholder’s interest (Jensen & Meckling, 1976). In addition, Monks and Minow (2011, p.415) suggest that the main challenge addressed by the advocates to agency theory regarding corporate governance is not far-fetched from “how to grant managers enormous discretionary power over the conduct of the business while holding them accountable for the use of their power”. Moreover, the agency

framework further advocates that corporate governance should be all about creating and monitoring the corporate mechanisms that are put in place by shareholders in order to control the managers to maximize shareholder wealth by mitigating agency loss (Bebchuk & Cohen, 2005; Bonazzi & Islam, 2007; Adegbite, Amaeshi & Amao, 2012).

The agency theory presents a different view on corporate diversification (Montgomery, 1994; Zhao, Hwang & Low, 2013). Based on the contributions from the study of Amihud and Lev (1981), several authors consider agency problems as the reasons for diversification discount (Afza & Nazir, 2014; Hoechle et al., 2012). Agency theory is based on the analysis principal and agent's conflicts (Jensen, 1986; Wu, 2012). The concept of this theory implies that risk averse managers do not pursue diversification for the benefit of the organization but rather go for decisions in order to reduce the threat of professional reputation or loss of job, resulting in agency cost (Amihud & Lev, 1981; Hoskisson & Hitt, 2011) or possible diversification discount (Mehmood, 2015). Accordingly, managers might be too desperate to implement diversification strategies (related and unrelated) as it might provide them with more incentives, compensation as well as control over resources and also assist them to stabilize the company's earnings and reduce the chances of bankruptcy for their own personal gains (Aggarwal & Samwick, 2003).

Every stakeholder of a firm creates value for the company. Since management are considered to be stakeholders of a firm, the manager is also included in this consideration. Thus according to this theory the manager is also affected by the outcomes of the firm. A positive firm performance will eventually make his position stronger. This will make the probability of him being fired smaller. Besides, this can also be applied to the topic

regarding managers' wealth maximization and firm performance. Thomsen and Conyon (2012) describe that the view of corporate expenditure of managers' change when they buy or receive company's stock. Thus changing the compensation structure or setting appropriate incentives for the managers can give positive results to the firm.

Jensen (2010) opine that the main contender to value maximization is stakeholder theory, which argues that managers should attempt to balance the interests of all corporate stakeholders, including not only financial claimants, but employees, customers, communities, and governmental officials. By refusing to specify how to make the necessary tradeoffs among these competing interests, the advocates of stakeholder theory leave managers with a theory that makes it impossible for them to make purposeful decisions. With no clear way to keep score, stakeholder theory effectively makes managers unaccountable for their actions (which helps explain the theory's popularity among many managers).

However, if value creation is the overarching corporate goal, the process of creating value involves much more than simply holding up value maximization as the organizational objective. As a statement of corporate purpose or vision, value maximization is not likely to tap into the energy and enthusiasm of employees and managers. Thus, in addition to setting up value maximization as the corporate scorecard, top management must provide a corporate vision, strategy, and tactics that will unite all the firm's constituencies in its efforts to compete and add value for investors.

On the other hand, the most frequently cited theory explaining the motives and benefits of corporate diversification strategy is the resource dependency view (Mehmood, 2015;

Marinelli, 2011). Based on the resource dependency postulations (Teece, 1982; Wernerfelt, 1984) corporate diversification is guided by the availability and capability resources of an organization. As a result, the organization diversifies into similar or different industries if it has enough resources and that could be utilize profitably in those industries (Barney, 1991; Martin & Sayrak, 2003). The issue of both related and unrelated diversification becomes more rational in markets where sale of excess resources and capabilities outside the company carries significant transaction costs (Mehmood, 2015). Therefore, diversification becomes the best way to utilize those resource for the benefit of the organization (Goddard et al., 2008).

By and large, an organization may possess various types of resources (tangible and or intangible) and capabilities that could be used for several beneficial purposes (Gruber, Heinemann & Brettel, 2010; Fatima, Rehman & Ali, 2011). For instance, in order to improve corporate performance, an organization could make use of its excess cash for lowering the prices, and or buying competitors or suppliers as well as exploit other tangible resources such as the use of same distribution systems and foreign offices for different business activities operating in different markets (Johnson, Scholes, & Whittington, 2011). However, the direction and the level of diversification depends on the package of its available resources and competences, which determines its generalizability (Yaghoubi et al., 2011). If the generalizability of those resources are greater, then the diversification level might be high (Teece, 1982). For instance, the excess resources in form of special knowledge drives an organization towards related diversification strategy enabling them to create economies of scope and improve firm performance (Palich et al., 2000).

The resource dependency theory assumes that the firm is embedded in its environment and depends on the resources from that environment to survive. The theory provides a theoretical basis for the role of corporate directors in the provision of resource and advice (Maigoshi, 2017). Unlike the agency theory which assumes the main role of directors is monitoring, resource dependency theory provides that the main role of corporate directors is the provision of resource function (Pfeffer & Salancik, 1978). The theory provides that the effectiveness of the board depends on the external resources the directors are able to bring to the board for the benefit of the firm.

Under the resource dependency theory, the board of directors is regarded useful as they provide the firm with important resources at lower costs and mediate the firm with external environment (Hilman & Dalziel, 2003; Hilman, Withers & Collins, 2009; Davis & Adam, 2010; Chen, 2014). Pfeffer and Sancik (1978) argue that directors provide four benefits to firm: i) provision of advice and counsel, ii) channeling of information between firm and the external environment, iii) preferential access to resources, iv) legitimacy. However, Hilman and Dalziel (2003) states that firms benefit most from directors when director provide both monitoring and resource functions. The theory assumes that directors with vast industry and business knowledge and multiple directorships are saddled with the responsibility of counsel and advice as they possess the requisite knowledge, expertise and experience to handle the duties (Maigoshi, 2017). Therefore well-diversified large boards handle the duties effectively (Pfeffer & Salancik, 1978; Hilman & Dalziel, 2003; Castro, De La Concha & Perinan, 2009).

Under TCE theory assumptions, it could be argued that a diversified organization might be more efficient compared to a single segment firm and could make better investment decisions because it has its own internal capital market (Berger & Ofek, 1995; Kuppuswamy & Villalonga, 2010) with the help of which, it could make successful allocation of resources across different businesses to improve its performance (Datta et al., 1991; Galván et al., 2007; Teece, 1982). Varanasi (2005) added that diversification could lead to creation of interaction economies through simultaneous supply of inputs and processes across different units.

Diversified organization could also gain performance benefits by combining businesses which have different flow of earnings (Berger & Ofek, 1995) or lowering variation in year by year cash inflows (Bhide, 1993). Diversification through backward and forward integration might lead to better performance through savings in production and transaction costs because in industries where the organization is working might be engaged in customer-supplier relationships (Fukui & Ushijima, 2006).

Market power advantages could also provide strong motives to strategic decision makers for pursuing product diversification strategy as highly diversified organizations can enjoy their market power in several ways in contrast to focused firms (Benito-Osorio et al., 2012; Park, 2010). For example, in contrast to a focused firm, a diversified organization with a variety of products and services possesses the opportunity to cross-subsidize a weak product using profits attained from a strong product, hence providing itself a better competitive advantage for the weak product (Johnson et al., 2008; Palepu, 1985).

Further, a diversified organization could use tactic of reciprocal buying and selling by developing favorable reciprocal arrangements with organizations which are its suppliers and customers at the same time (George, 2007; Palich et al., 2000). In this direction, an arrangement could be established where a company's supplier could be purchasing certain outputs from one of the business unit being acquired by the company and this diversification would result into multiple relationships with other Organisations (buyers or suppliers) providing it greater market power and high performance (George, 2007; Goddard, McKillop, & Wilson, 2008).

Moreover, diversified organizations might use income generated through one market in another market for the purpose of predatory pricing i.e. price cutting (Goddard et al., 2008; Klier, 2009). By using this strategy, a diversified organization could create entry barriers for new entrants, and push existing rivals out of the market, thus bringing itself a strong strategic position as well as safer business environment in concerned industries (Palich et al., 2000; Saloner, 1985). Another advantage of market power could be possible in form of 'mutual forbearance', according to which multiproduct Organisations would compete less severely amongst themselves when they are competing in number of geographic segments (Martin & Eisenhardt, 2001). However, according to Bernheim and Whinston (1990), this situation might also apply to single product firms. Overall, the views expressed herein support the argument that related or unrelated diversification strategy is beneficial for an organization as it provides increased market power.

Based on the theoretical perspective, the empirical findings on how paramount the corporate governance mechanisms and diversification are to be structured to boost

corporate performance and serve the interest of shareholders using diverse theoretical views however remain inconclusive (Combs, Perryman & Donahue, 2007). Correspondingly, Jackling and Johl (2009) and Arosa, Iturralde and Maseda (2010) proclaim that one theory alone cannot adequately explain the firmness of corporate governance mechanisms, thus integrating multiple theories may provide better understanding of dynamism of corporate governance. Hence, this justifies the use of agency theory, stakeholder theory, resource dependency theory, TCE and market power view as a guide to this research work. Studies on the roles of corporate board is gaining more attention and importance (Mohammed, 2012; Hassan, Marimuthu & Kaur Johl, 2015; Zabri, Ahmad & Wah, 2016; Krishnan & Mohd Amin, 2017). Several theories attempt to explain the issue of board roles, namely agency theory (Mat Rabi et al., 2010; O'Connor & Rafferty, 2012) resources dependency theory (Hillman, & Dalziel, 2003; Krishnan & Mohd Amin, 2017) , stewardship theory (Davis, Schoorman & Donaldson, 1997; Mason, Kirkb & Bryde, 2007) and class hegemony (Baker, 2010; Mahadeo, Soobaroyen & Hanuman, 2012). Since the study is guided by all the affirmation theories (agency theory, stakeholder theory, resource dependency theory, TCE and market power view), it makes its contribution to these underpinning theories by investigating the effects of corporate board, diversification strategies on firm value in the context of emerging economy of Malaysia. The research framework and description of variables are shown in figure 3.1.

3.3 Research Hypotheses

The statement of each of the hypotheses proposed in this study is presented in this section. The hypotheses statements are formulated on the basis of research questions and research objectives listed in chapter one, literature review discussed in chapter two, and theoretical framework presented above. Moreover, different set of hypotheses are formulated for testing because each variable (independent, dependent as well as moderating variable) consists of sub variables. A brief detail and justification is added with every hypothesis to clarify its need and significance for this study.

3.3.1 Board Size

One of the main proxies to corporate governance is board size, which means total number of directors on the board. Board of directors has a responsibility to ensure the implementation of corporate governance practices (Shleifer & Vishny, 1997). According to Malik et al. (2014) the relationship between board size and firm value is still a fundamental issue for researcher. Some authors suggest that on average 5 to 16 members to be present at the board of an organization (Yasser et al., 2015). The two schools of thoughts, large board and small size board, both have their own advantages and criticisms. But empirical research results are mixed across various countries and industry dynamics, and still it is a matter of research which school of thought to be followed in a particular situation (Yang et al., 2009). If the academic research is broadly analyzed, the imperial results in developing countries show a mix results on association of board size and firm value (Nazir et al., 2009).

The advocates of small board size in organization (Lipton & Lorsch, 1992; Jensen, 1993; Yermack, 1996; Mak & Kusnadi, 2005) believe that, small board results in better for organizational performance, higher firm value and oversight. Smaller boards have the abilities to better communicate, coordinate and make decisions more, effectively (Khan, 2017). According to Yasser et al. (2011) the limited number of directors in the board has a positive impact on firm value. Similarly result were drawn in research conducted by Yermack (1996), Mak and Khusnadi (2001), Rouf (2011) and found in their studies a negative relationship between board size and firm value. Notwithstanding this, Coles et al. (2008) use the sample of firms in the IRRC (Investors Responsibility Research Center) database and arrived at U-shape relationship between board size and firm value. This suggests that neither large board size nor small board size is optimal for a firm. The advocates of large board size suggested that firms that are large in size and complex require more expertise of their directors. So the presence of large board and more representation of directors are prerequisite for smooth operations and control.

However, contrary to smaller board size in organization there is constant debate and support from empirical results to have large board in organization. Coleman and Biekpe (2006) argue that in developing countries like Ghana the board size and firm value have a positive relationship. Van den, Berghe and Levrau (2004) argued that resource dependency theory favors the large board size that increases the value of firm because members have managerial talent and they perform their duties effectively. There is also a view point that large board size has more control on top management and directors can prudently monitor the management performance and duties, which will eventually increase the value of the firm (Abdullah et al., 2012). Based on the concept of resource dependency theory, large

board contains many people with diverse knowledge, skills, experience and expertise which imply strong monitoring and advising roles, thus promoting corporate transparency that will eventually increase firm value (Samaila, 2015). In view of this, the next hypothesis is formulated as thus;

Hypothesis 1 (H₁): Board size has a positive effect on diversification value.

3.3.2 Board Independence

Based on the agency theory, several studies document that the presence of independent directors on the board minimizes both type I and type II agency problems (Fama & Jensen, 1983; Adams et al., 2008; Crespi-Cladera & Pascual-Fuster, 2014; Maigoshi, 2017), and their adequacy protects the interest of all stakeholders (Lo et al., 2010; Mallin et al., 2015). Resource dependency theory suggests that outside directors promote firm value through counselling and advising role (Pugliese et al., 2014). Germain, Galy and Lee (2014) state that the issue of independent directors has been gaining much attention in recent years and notice an upward trend of independent directors in many corporate boards. Several studies conducted on board independence establishes a positive relationship between the number of independent directors and firm value (Cybinski & Windsor 2013; Liu, Miletkov, Wei & Yang, 2015). In view of the aforementioned, the next hypothesis is stated as;

Hypothesis 2 (H₂): Board independence has a positive effect on diversification value.

3.3.3 Audit Committee Independence

Based on agency and resource dependency theories, audit committee plays important role in explaining firms' financial practices. Audit committee has a fiduciary responsibility of monitoring compliance with all related financial requirements (Al-Akra, Eddie & Ali 2010; Brochet & Srinivasan, 2014). Generally, the presence of audit committee is found to increase the firm transparency and mitigates agency costs (Al-Najjar & Abed, 2014; Cai, Hillier, Tian & Wu, 2015). The degree of independence in the audit committee affects the quality of the oversight of firm financial reporting process (Black & Kim, 2012; Li, Mangena & Pike, 2012). Abbott, Parker and Peters (2004) confirms that the presence of the independent audit committee with strong monitoring activities decreases the tendency of producing misleading financial reports.

Nekhili and Cherif (2011) use 3SLS simultaneous model on 85 Paris-listed firms to investigate the effect on audit committee independence on related party transactions. The results show that the degree of independence of audit committee influences the level of firm's related party transactions, hence affecting firm value. Similarly, Cai et al. (2015) investigate the role of audit committee in mitigating the effect of agency cost of ownership structure. The findings provide evidence that audit committee independence is valued by shareholders and mitigates the agency costs associated with ownership structure. Based on this study hypothesizes that;

Hypothesis 3 (H₃): There is a positive relationship between audit committee independence and diversification value.

3.3.4 Audit Committee Size

According to the resource dependence theory, a larger audit committee means the members can bring more resources to the firm, such as experience and expertise, which contribute to the audit committee's effectiveness in monitoring management, hence leading to high earnings quality. The Cadbury Report (1992) and the Smith Report (2003) stipulate the number of audit committee members must be at least three; the Sarbanes–Oxley Act (2002) also mandates a minimum of three members in the audit committee. Buchalter and Yokomoto (2003) recommend that audit committees should compose of three to five members although it is generally based on the firm's size. The MCCG (2012) recommends there should be at least three non-executive directors in the audit committee, a majority of whom should be independent.

Empirical studies provide evidence that audit committee size is related to increase in firm value (Lin, Li & Yang, 2006; Garcia, Barbadillo & Perez, 2010). Additional evidence from Malaysia by Ahmad-Zaluki and Wan-Hussin (2010); and Ismail, Adibah, Dunstan and Zijl (2009) find a significantly positive relationship between audit committee size and earnings performance. However, Abbott, Parker, Peters and Raghunandan (2003); Baxter and Cotter (2009); Adiguzel (2013); and Hussein and Kumardin (2015) find an insignificant association between audit committee size and firm performance. A more recent study conducted by Kipkoech and Rono (2016) revealed that audit committee experience and audit committee size has a significant effect on firm value. In view of the ongoing debate, the subsequent hypothesis is thus;

Hypothesis 4 (H4): There is a positive relationship between audit committee size and diversification value.

3.3.5 CEO Expertise

Based on the agency theory laid down emphasis on the opportunistic behavior of managers, since they try to consider their self-interest at the detriment to that of shareholders (Afza & Nazir, 2014) Therefore, the cost of resolving this problem upturns due to the involvement of several corporate governance mechanisms and other monitoring systems and the dashing out money and monetary benefits managers among others. Additionally, Eisenhardt (1989) revealed that the incentive schemes given to managers may assist to maximize shareholders interest and also the introduction of outcome based incentive contract that reduce managerial opportunism, especially when the CEO has the interests with the shareholders through more suitable designed incentive plan.

The level of CEO expertise has been found to influence the success and otherwise of the numerous decisions and strategies he takes in a firm. Custodio and Metzger (2013) investigates the relationship between CEO expertise and firm market value of 1500 standard and Poor (S&P) firms. Using the sample of CEO- firm years' observations, the results show that financially expert CEOs increase the market value of the firms. Financially expert CEOs take favorable business strategy business decisions related to cash holding, share repurchase and so on. Accordingly, Custodio and Metzger (2013) and Huang et al. (2015) document that firms that focus on the industry in which they possess managerial expertise achieved significant improvement in performance. The improvement is more for the firms with CEO with much experience in that industry.

Consistently, Haislip and Richardson (2015) find the IT expert CEOs make more accurate estimations that lead to more accurate earnings forecast. Correspondingly, Dubocage and Galindo (2013) conclude that venture capitalists retain the CEOs with core business expertise. Based on the revelations from prior studies, the next hypothesis is thus:

Hypothesis 5 (H₅): There is a positive relationship between CEO expertise and diversification value.

3.3.6 Risk Management Committee

Consistent with the risk based approach, a company that establish RMC as one of the board exhibits a greater awareness of the importance of risk management and control (Beasley, Clune & Hermanson, 2005; Yatim, 2010). Since the monitoring by the board of directors has heightened through a stringent risk management procedure, one can contend that the financial reporting quality and risk management and mitigation programs of corporations has been greatly enhanced (Yatim, 2010). Therefore, in the context of corporate governance best practices, this study examines the relationship that exist between RMC and firm performance. Although, a board that is more independent, with enough expertise and duteous is likely to set up a standalone RMC to oversee and control various risks faced by the firm (Yatim, 2010).

RMC is an important element of corporate governance since it provides a means of realizing corporate objectives and monitoring the performance of an agent by a principal (McNutt & Demidenko, 2010). Whereas, Gates et al. (2012) stated that the RMC monitors the level of risk whilst attempting to maximize returns by advising the board of current risk

exposures and future risk strategies. Which is in line with MCCG issued by Securities Commission and Bursa Malaysia listing requirements. Likewise, the studies of Zhao, Hwang and Low (2013) and Culp (2002) considered risk management as consisting of specific efforts that establish a buffer or contingency to absorb economic effects and impose controls that will mitigate the extreme losses of a company. Although, the MCCG, (2012), mandated the board to determine the company's level of risk tolerance and actively identify, assess and monitor key business risks to safeguard shareholders' investments and the company's assets. While many advocates of RMC have highlighted the numerous benefits of a stand-alone committee to oversee risk, the empirical finding in this association remains vague and narrow. Among the RMC related researches, Brown et al. (2009) conducted a thorough review of risk management in the Australian biotechnology companies. Subramaniam et al. (2009) examined how the establishment of an RMC is associated with a firm's characteristics and board factors, while Yatim (2010) also performed a similar research in the Malaysian context. Ng, Chong and Ismail (2012) further give an insight into managing risk taking among insurance companies in Malaysia. Bugalla et al. (2012) on the other hand, proposed a new model of governance and risk management for financial intermediaries. How well an RMC in place could serve its purpose in minimizing the tendency to take risk remains the critical point. It is believe that an RMC continues to play an integral part in various risk issues that influence the success of the operation, particularly after the regulatory change.

Studies (Aebi, Sabato & Schimid, 2012; Ong et al., 2015; Bhuiyan et al., 2017) on the link between the RMC and performance are inconclusive. Cummings and Patel (2009) noted that risk management and financial activities improve the efficiency and consequently the

performance of a firm by reducing costs. Contradicting this, Tufano (1996) found little empirical support for risk management practices as a means of maximizing shareholder value. The study of Tufano (1996) discovered that risk management practices of firms, such as hedging to reduce their exposure to risk, are more likely to be related to managerial risk aversion than maximizing shareholder value. In Malaysian context, Yatim (2010) studied the effect of setting up RMC in 690 publicly listed companies in Malaysia in 2003. The study discovered a strong relationship between the existence of a RMC and board structures, thereby demonstrating a stronger commitment and awareness of the importance of an internal control system. RMC have made a significant contribution to ensuring that risks are mitigated effectively, thereby improving corporate performance.

However, the study of Ong et al. (2015) reveals that setting risk management committee made no difference in financial performance. While the study of Aebi, Sabato and Schmid (2012) investigates the impacts of risk management-related corporate governance mechanisms in bank performance during the financial crisis. The results shows a collinear relationship with performance, whereas the coefficient on number of meetings of the risk committee is positive and significant. RMC have made a significant contribution towards ensuring that risks are mitigated effectively, thereby improving corporate performance. Similarly, the hypothesis is formulated as.

Hypothesis 6 (H₆): Risk management committee positively affect diversification value.

3.3.7 Tenure of Independent Directors

The essence of agency problem is that self-centered managers may waste corporate resources over noneconomic, value destroying ventures and activities (Jensen & Meckling, 1976). The clear implication of research agenda for corporate board from an agency theory perspective is that monitoring should be intensified (Aduda, Chogii & Obara, 2013). It would therefore, means that corporation should have proper regulation of board mechanism on independent directors' tenure. Most of codes on best practices so far advanced by different bodies and countries have learnt towards implementing the agency theory recommendations. However, independent directors of Malaysian PLCs are required to serve for only cumulative term of nine years. Upon completion of the nine years, an independent director may continue to serve on the board subject to the director's re-designation as a non-independent director, the assessment criteria for independence of directors should also include tenure (MCCG, 2012).

Though, looking at it from an empirical perspective, the study of O'Reilly and Caldwell (1981) and Xie (2014) postulate that directors' organizational commitment increases in tenure. Longer tenure directors may have high job satisfaction and they are less likely to reverse their job acceptance. Thus, extended directors' tenure can enhance the commitment of directors to fulfill their duties and reduce their turnover. In essence, long-tenure directors possess higher commitment and willingness to work better. They also possess greater experience, expertise and reputation which are beneficial to the firm (Xie, 2014).

On the other hand, studies by Bebchuk and Cohen (2005) suggest that management may also use their power to influence the nomination process of directors as well. Independent

directors with strong personal ties with the management are more likely to be re-appointed and survive long term. Long tenure increases a director's knowledge of the firm, allowing shareholders' interests to be better served, these directors will not operate independently because they already possess strong personal ties with the management (Wilson, 2016). This will also encourage the controlling shareholders to expropriate resources from the firm without significant check and balances from the independent directors at the expense of the minority shareholders (Vafeas, 2003).

In addition, long tenure directors are less mobile and less employable (Vafeas, 2003). As business operations become more sophisticated and frequently changing, long tenure directors increasingly find it difficult to keep track of the changes in technology, financial dealings, and business strategies as compared with their new counterparts (Musteen & Datta, 2010). Similarly, the former also lack talent to deal with new issues. However, the longer the director serves the company, the more comfortable the director is with the company and the director's performance may decrease (Ishak, 2004). Based on the above arguments, the next hypothesis is stated as:

Hypothesis 7 (H7): The tenure of independent directors has negative impact on diversification value.

3.3.8 Diversification Strategy

The basic premise of resource dependency theorists, is that corporations depends upon one another for access to valuable resources and therefore, seek to establish links in an attempt to regulate their interdependence (Hung, 1998; Marinelli, 2011). Accordingly,

diversification is being guided by resources and capabilities of an organization (Teece, 1982; Wernerfelt, 1984). Consequently, the organization diversifies into similar or different industries if it possesses excessive resources and capabilities that it could utilize profitably in those industries (Barney, 1991; Martin & Sayrak, 2003). Thus, related and or unrelated diversification becomes more rational in markets where sale of excess resources and proficiencies outside the organization conveys significant transaction costs and therefore diversification becomes the best way to utilize them within and outside the organization (Goddard et al., 2008).

The study of Mehmood (2015) further revealed that the quest for diversification strategy is mainly based on organizations' strategic capability defined by mixture of its unique resources and core competences, and the direction of diversification strategy depends upon the nature of resources and the know-how it possesses. In the event, whereby the resources are related, organization would enjoy financial economies and or other internal efficacies through related diversification. Alternatively, if the resources are not related with each other, the motives and benefits available to organization would be in form of synergy effects or economies of scope through unrelated diversification.

However, agency theory presents alternative perspective on diversification strategy (Montgomery, 1994; Zhao, 2010). Many scholars consider agency problem as the main reason for diversification discount (Afza et al., 2008; George, 2007; Hoechle et al., 2012). This concept implies that risk averse managers do not pursue diversification for the betterment, of organization, instead, managers undertake diversification decision in order to reduce to their professional reputation or job loss, therefore, resultant in agency cost

(Hitt et al., 2011; Lane, Cannella Jr., & Lubatkin, 1998) or possible diversification discount.

Meanwhile, managers might be frantic to implement diversification strategies as it might provide them greater incentives, compensation and control on the overall resources as well as assist them stabilize company earnings and reduce the chances of bankruptcy for their personal benefits (Aggarwal & Samwick, 2003; Jensen, 1986). The agency cost became higher when principal does not share same interest with the agency as well as being unaware of the activities of agent (Lupia, 2001; Nyberg, Fulmer, Gerhart, & Carpenter, 2010). However, agency cost could be reduced, via alignment of managerial incentives or increase in effective control and monitoring by the boards or principals (Bryant & Davis, 2012).

A comprehensive discussion of studies supporting positive effects of diversification (Pandya & Rao, 1998; Ishak, 2004; Miller, 2006; Mishra & Akbar, 2007a; Kuppuswamy & Villalonga, 2010; Ishak & Manaf, 2013) and negative effects of product diversification (Braakmann & Wagner, 2009; Hoechle et al., 2012; Ibrahim & Kaka, 2007) has been presented in the previous chapter. Moreover, the discussion also included review of studies supporting curvilinear effect of diversification on performance (Galván et al., 2007; Liu & Hsu, 2011) as well as analysis of studies stating that diversification strategy has no significant effect on performance (Montgomery, 1985; Chang & Thomas, 1989; Lloyd & Jahera Jr., 1994; Colak, 2010; Marinelli, 2011; Patrisia & Dastgir, 2016).

A critical analysis of these studies reveals that there are more studies stating that diversification had some sort of effect on performance (Choe et al., 2014; Ishak & Napier,

2006; Villalonga, 2004) as compared to studies (Zahavi & Lavie, 2013; Patrisia & Dastgir, 2016) concluding that there was no effect of diversification on performance. Moreover, greater studies have supported linear relationship between product diversification and performance as compared to studies supporting curvilinear relationship between the two. Among those studies (Galván et al., 2007; Liu & Hsu, 2011) which state that product diversification had certain impact on performance, there are considerable studies proving positive effects of diversification on performance as well as there are sizable studies proving negative effects of diversification on performance. Therefore, there lies greater ambiguity about whether diversification is either a useful strategy or not. In light of this analysis, an initial hypothesis concerning the effect of diversification strategy on firm value is presented below:

Hypothesis 8 (H₈): There is a positive relationship between total diversification and diversification value.

3.3.8.1 Related Diversification Strategy

This strategy deals with the company's expansion into new line of product and markets which is still within the existing strategic business capability (Mehmood & Haim, 2015). As such companies company's new line of business activities are related with the existing undertakings (Lahovnik, 2011) and the businesses are similar to each other in terms of input and operational requests (Teece, 1982). In relation to the specific motivations for diversification, most corporations decide to diversify into related businesses in order to achieve economies of scope (Almudena, 2016). Therefore, this strategy seems to be the result of a profit seeking attitude to thrive and survive in the business context due to

economies of scope which can lead to a reduction in total costs and an increase in firm profitability and performance (Galan & Sanchez-Bueno, 2009). In particular, related diversification enable a firm to share and transfer critical success factors across different businesses leading to efficiencies in resource allocation and ultimately to cost advantages (Wan, Hoskisson, Short & Yiu, 2011). Moreover, firms can also reduce total costs by exploiting interrelationships between businesses based on technical and managerial skills and functional specialization (Zhou, 2011).

Collins and Montgomery (2008) believe that related diversification involves building shareholder value by capturing cross business strategic fits. The combining of resources creates new competitive strengths and capabilities (BCG, 2006). Related diversification may involve use of common sales force to call on customers, advertising related products together, use of same brand names and joint delivery. On the other hand, Thompson and Strickland (2006) believe that many companies decide to diversify into any industry or business that has good profit opportunities. As specified in the previous chapter, several past studies established linear relationship between related diversification and corporate performance. Following the discussions, the hypothesis is stated thus:

Hypothesis 8a (H_{8a}): There is a positive relationship between related diversification strategy and diversification value.

3.3.8.2 Unrelated Diversification Strategies

Unrelated or conglomerates diversification deals with company's expansion beyond its current strategic capability (Robinson & Pearce, 2011) whereby its new business and or

subsidiaries have little or no relatedness with the old or existing businesses (Mehmood & Hilman, 2013). In contrast, the unrelated diversification strategies are mostly motivated by empire building desire by some managers (Almudena, 2016). Although unrelated diversification may involve some unique benefits resulting from financial synergies, such as risk reduction and coinsurance, this strategy tends to be an easy alternative for rapidly increasing firm size (Colpan & Hikino, 2005; Giffin, 2013). On the other hand, corporate growth is more beneficial to top managers whose pay, status and job security tend to be determined more by the firm size rather than its profitability (Aggarwal & Samwick, 2003; Laeven & Levine, 2007). Consequently, due to the nature of firms size in developing nations as compared to the developed countries, the pursuit of managerial self-interest via empire building seems to be the most influential motive for their conglomerates strategies (Almudena, 2016). Therefore, the unrelated diversification strategies for these nations may be considered a strategy for enhancing firm size and benefits for top managers, subject to a minimum profit constraint (Benito-Osorio et al., 2012).

The literature on conglomerates clearly depicts that reduction of overall company risk and increase in profitability have been main motives behind this strategy (Grant et al., 2011). In contrast to focused companies or related ones, unrelated diversifiers have better position to create financial synergies by transferring capital across different businesses and through operating various businesses with different risk profiles (Berger & Ofek, 1995; Galván et al., 2007). In a huge conglomerate, these benefits are easily attainable through large internal capital market capable of generating substantial financial economies (Hoskisson et al., 2009). Johnson et al. (2006) noted that in most cases companies that pursue unrelated diversification strategy nearly always enter new businesses by acquiring an established

company rather than by forming a startup subsidiary. The basis for this strategy is that, growth by acquisition translates into enhanced shareholder value faster and the payback period is quicker (Mehmood, 2015). Thus the following hypothesis is formulated as:

Hypothesis 8b (H_{8b}): There is a positive relationship between unrelated diversification strategy and diversification value.

3.3.9 Managers' Wealth Maximization

Based on the agency theory proposition that when ownership is separated from the control of a large firm, the manager acts as an agent on behalf of the principal, thereby, is inclined to creating moral hazards such as skirting and seizing wealth at the expense of the principal (Afza & Nazir, 2014). This issue of divergence in agents' actions and principals' interest leads to agency problem, when managers disregard the concerns of their principals and consider their self-interest on precedence line and collect private benefits by venturing into diversification activities for their personal wealth maximization, building empires and enjoying perquisites (Shliefer & Vishny, 1997). Consequently, at this point, there were questions on how to align managers' task with shareholders' interest? An answer to this interrogation is to give right and sufficient incentives to managers that must be linked to their performance of putting their best in favor of their principals (Berle & Means, 1932).

Additionally, Olaniyi (2019); Raithatha and Komera (2016). gave similar opinion that incentives schemes for managers help to maximize shareholders' interest and also introduced out-come based incentive contract that reduce managerial opportunism, particularly when CEO has the same interest with the shareholders through an

appropriately designed incentive compensation plan. However, contradictory views also exist on this issue. Some researchers consider managerial compensation as part of agency problem. They claimed that it gives more power to agents whereby compensation is only a fractional remedy of agency problem (Bebchuk & Fried, 2003). Alternatively, the ultimate solution the ultimate solution to this issue is to create a relationship between compensation and firm performance which referred to as pay for performance (Rupp & Smith, 2002).

However, this study use managers' wealth maximization to moderate the relationship between diversification strategies and firm performance. It has been contended by previous researchers that better insight could be gained into diversification – performance relationship with the inclusion of additional variables (Daud et al., 2009; Gary, 2005; Marinelli, 2011) or moderators (Martínez & Fernández, 2008) into the relationship. Importantly, scholars suggested that researchers should include important contingency variables in their research frameworks when the purpose is to study relationship between related diversification strategy and performance, as well as to study unrelated diversification strategy and performance (Datta et al., 1991; Ravichandran et al., 2009). In addition, the study of Mehmoud (2015) considered corporate parenting as a crucial issue related to diversification strategies. Though, the study attempted to reconcile the inconsistencies concerning diversification and performance relationship by focusing on the moderating effect of corporate parenting roles on the relationship. Most importantly, Li, (2008) and Choe et al. (2014), suggested the use of “managers' wealth maximization” as a moderating variable in diversification strategies and performance relationship.

Manager's wealth function comprises of both monetary rewards, such as salary, bonus, options, and non-pecuniary benefits associated with managing a larger corporation, for example, prestige, power, and perquisites such as company cars, offices and so on. Especially, the non-monetary rewards are the benefits that diversification provides to managers and the shareholders do not enjoy (Li, 2008). Diversification obviously provides managers an avenue for increased compensation and may serve as a motive for increased diversification in order to maximize their monetary gain (Hoskisson & Hitt, 1990). On the basis of these discussions therefore, managers' wealth maximization is used to moderate the relationship between types of diversification strategies on one hand and corporate value on the other hand. Therefore, the following hypothesis is formulated as.

Hypothesis 9a (H_{9a}): Managers' wealth maximization positively moderates the relationship between related diversification strategy and diversification value

Hypothesis 9b (H_{9b}): Managers' wealth maximization positively moderates the relationship between unrelated diversification strategy and diversification value.

3.4 Population of the Study

This study investigates the effect of corporate board and diversification strategy on diversification value. It further tests whether managers' wealth maximization moderates any relationship between diversification strategies and corporate performance. The unit of analysis in this study is diversified Malaysian non-financial Public Listed Companies (PLCs). The word 'company' used in this research for all Malaysian companies actually represents a diversified companies with multiple segments.

The population frame for this study consisted of all diversified PLCs listed on Bursa Malaysia Main Market that reported the activities of multiple segments for the required period of time. Companies listed only on the Main Market of Bursa Malaysia are included in the population frame as there are various differences in the listing requirements for companies for Main Market versus ACE Market (Mehmood, 2015). Hence, to maintain homogeneity among companies, only Main Market companies are considered in the study.

Malaysia, companies are required by Malaysia Financial Reporting Standard (MFRS) to report their business segments detail as per MFRS8 issued by MASB/IASB. A company is categorized as diversified company if the number of product segments disclosed under operating segments is more than one (David et al., 2010; Ishak & Napier, 2006; Mehmood, 2015; Palepu, 1985; Santalo & Becerra, 2008). Whereas, companies reporting the activities of only one segment are considered as focused companies and therefore excluded from the sample of the study.

3.5 Sampling and Source of Data

The sampling frame for this study consists of non-financial public companies that are listed in Bursa Malaysia as at the end of 2017. Financial institutions were excluded because they are subjected to a regulatory framework that does not apply to other listed companies. PLCs are chosen because they have several advantages over non-listed companies. The main reason is that PLCs have published annual reports that are publicly available and can be assessed using the Bursa library or its website. Additionally, the published reports of PLCs are presented in a more uniform way and have more complete data because they are subjected to certain regulations by Bursa Malaysia as well as the Companies Act 2016. In

addition, the use of PLCs enables comparisons with prior researches in Malaysia because most studies use the PLCs.

This study relies on single year data in order to test the diversification status of the diversified public listed companies, this is also in consistent with the work of Ishak (2004), Lins and Servaes (2002), Chen and Ho (2000), Ahmad et al. (2003), Goddard, Molyneux and Wilson (2004), Lang and Stulz (1994), Miller (2006) and Ishak and Napier (2006). A short time period is desirable because strategic plans frequently changes overtime, (Eukeria & Favourate, 2014; Mehmood, 2015), therefore in diversification studies, a shorter time period is desirable (Daud et al., 2009). Hence this study examines the diversification status of the sampled listed companies, since the diversification strategies can be frequently change within the shortest possible time by the companies depending on the strategy that is more rewarding and suits the companies' diversification motive.

Meanwhile diversification is being guided by resources and capabilities of an organization (Wernerfelt, 1984). Consequently, the organization diversifies into similar or different industries if it possesses excess resources and capabilities that it could utilize profitably in those industries (Martin & Sayrak, 2003). Thus, related and or unrelated diversification becomes more rational in markets where sale of excess resources and proficiencies outside the organization conveys significant transaction costs and therefore diversification becomes the best way to utilize them within and outside the organization (Goddard, McKillop, & Wilson, 2008).

Corporate diversification strategies can differ significantly between companies, not only in the number of businesses in which each competes, but also in the nature of the relationships

between those businesses. As alluded previously, certain scholars have noted that a firm can vary either in the level (extent) of diversification or in the nature (type) of diversification (related or unrelated). The level of a firm's diversification can be operationalized very simplistically by counting the number of businesses in which the firm operates. The more businesses in which a firm competes, the higher a level of diversification it is considered to have. More robust operationalization (e.g., the entropy or concentric measure) of the extent of diversification are based on the distribution of the firm's revenue across its various businesses.

Another explanation for relying on 2017 year data, is in relation to the introduction of the new MCCG 2017 code which supersedes the 2012 MCCG, sets out the broad principles and specific recommendations on structures and processes which companies should adopt in making good corporate governance an integral part of their business dealings and culture. The MCCG 2017, like all corporate governance codes, advocates the adoption of standards that go beyond the minimum prescribed by regulation. Listed companies are now required to provide a meaningful explanation in their annual reports on the manner in which the practices are applied and, where alternative practices are adopted to meet the intended outcome, to provide reasons for such alternatives and where appropriate, the timeframe required for its implementation. The first set of companies required to report on conformance with the MCCG 2017 in their annual report are companies with financial years ending 31 December 2017 (Rajah & Tann, 2017).

Further justification for the determination of year 2017 depends on the recently introduced Companies Act 2016 which supplant the earlier utilized companies' Act 1965. The new Companies Act of 2016 came up with different changes and reforms, some of which are;

prescribes the minimum number of directors for a public company is two resident directors, provides that the fees of the directors, and any benefits payable to the directors of a public company, or of a listed company and its subsidiaries, shall be approved at a general meeting, abolish the maximum age for directorship, enhance internal control, corporate governance and corporate responsibility, statutory declaration by promoters / directors to be replaced with statement of compliance.

The year 2017 was picked as it was the most recent financial year for all listed companies' published annual reports were available at the time when data collection was started after the gazette of the Companies Act 2016. PLCs have a couple of months after their financial year-end to publish their evaluated annual report, information for 2018 could not be gathered since not all organizations' annual reports finished in 2018 were accessible at the time of data collection. Hence, the selection of 2017 year financial data of public listed companies is viewed as the most reasonable for this study. The study utilized hand-gathered information from secondary sources of companies' annual reports.

3.6 Variable Measurement and Data Collection

Data measurement is an important aspect of variable definition, based on the definition of the relationships between the variables (Ishak, 2004). Therefore, in this study, in order to secure the validity of variable measurement, the definition of the variables is carefully provided from the review of prior literatures relevant to this study. Hence, the variables for corporate board structures, diversification strategies, diversification value and managers' wealth maximization are defined, measured and collected thus.

3.6.1 Tenure of Independent Director

Consistent with the approach under the 2012 MCCG, the 2017 MCCG discourages an independent director from serving for more than 9 years. Retention of an independent director above 9 years will require shareholders' approval, whereas retention of an independent director above 12 years will require shareholders' approval through the two-tier voting process. The voting process can either be by large shareholders and or voting by other shareholders. Large companies are discouraged from retaining an independent director for more than 12 years. The two-tier voting requirement will be effective only for resolutions to be tabled at general meetings. This tenure of independent director is measured with the total number of independent directors in the Malaysian publicly listed companies that serve a tenure of not more than 9 years.

3.6.2 Risk Management Committee

The MCCG (2012) mandated the board to determine the company's level of risk tolerance and actively identify, assess and monitor key business risks to safeguard shareholders' investments and the company's assets. In order to achieve the provision of the MCCG (2012) the risk management committee is measured base on the dichotomy coded as '1' if a risk management committee exists and as '0' if otherwise.

3.6.3 Board Size

The number of directors on the board (or board size), therefore, is a critical factor that influences the performance of a company. The board acts on behalf of shareholders, and is considered as a major decision-making group. The complexity of decision-making and

effectiveness is largely affected by the size of board. Board size is measured by the total number of directors on the board. This is consistent with the studies of Kumar and Singh (2013) and Khan (2017).

3.6.4 Audit Committee Independence

As mentioned before, independence is an important condition to be met by the members of audit committees. The independence of the audit committee refers to the number of independent non-executive directors on the audit committee. Audit committee independence is measured by the proportion of independent director on the audit committee (Klein, 2002; Goh, 2009; Al-ebel, 2013).

3.6.5 CEO Expertise

CEO expertise is coded by assigning '1' when CEO is considered financial expert and or is a member of accounting professional body and or possesses a finance-related academic qualification, and '0' if otherwise (Custodio & Metzger, 2013; Haislip & Richardson, 2015).

3.6.6 Audit Committee Size

Audit committee size in this study is measured with the aggregate number of audit committee members available in the audit committee. This measurement is consistent with previous studies conducted by Bala and Kumai (2015), Al-ebel (2013), Goh (2009), Gan et al. (2008) and Li et al. (2008).

3.6.7 Board Independence

The board independence in this study is measured as the proportion of independent director present on the total board of directors. This measurement is consistent with the study of Maigoshi (2017) and Al-ebel (2013).

3.6.8 Diversification Strategies

The measurement of diversification strategy have been a topic of discussion and dispute over the previous years (Mehmood, 2015), prior studies have used various different ways for computing companies' extent of diversification strategies. Whereas diversification strategies range from categorical to continuous measures (Asrarhaghighi et al., 2013; Klier, 2009) with each one serving a particular purpose. Continuous measures of diversification strategy is better since they provide ratio data and therefore, they can be considered to be more accurate in calculating degree or extent of diversification (Chari, Devaraj, & David, 2008b; Almudena, 2016).

Furthermore, the research is more focus with making categories of related diversifiers and unrelated diversifiers for testing the formulated hypotheses. Hence, given the objective of this study and the nature of analyses, this study rely on the 'Entropy Measure' of diversification strategy. The use of entropy measure is well-known in diversification literature and a number of prior researches used this measure of diversification in related studies (Martínez-Campillo, 2008; Ravichandran et al., 2009; David et al., 2010; Kahloul & Hallara, 2010; Marinelli, 2011; Shukla & Dwivedi, 2016). Though the entropy measure is not only restricted to the measurement of the degree of company's total diversification,

but also have the ability to measure both the degree of related unrelated diversification (Mehmood, 2015). Based on comparison of a company's score of related and unrelated diversification, a company can be categorized as either "Predominantly Related Diversifier" or "Predominantly Unrelated Diversifier". As a result, entropy measure provides continuous data as well as possibility of categorizing companies into two categories. Accordingly, the entropy measure provides the following three measurements or scores: (i) Entropy measure or score of total diversification (TD). (ii) Entropy measure or score of related diversification (RD). (iii) Entropy measure or score of unrelated diversification (UD).

The following are the expression of formulae for the three components of entropy measure as given in Palepu (1985), Chakrabarti, Singh and Mahmood (2007) and Mehmood (2015).

1. Entropy Measure of Total Diversification (DT) can be calculated as:

$$TD = \sum_{i=1}^N P_i \ln(1/p_i)$$

Where;

TD = Total product diversification score

P_i = share of *i*th segment in total sales of the firm.

N = number of industry segments where a firm is working.

2. Entropy measure of related diversification can be calculated as:

$$RD = \sum P_j^{RD_j}$$

RD = Total Related Diversification Score (Actually, RD represents weighted average of related diversification within all industry groups).

P^j = share of jth group sales in the total sales of the firm and

M = Number of industry groups where a firm is working.

RD_j above can be calculated as:

$$RD = \sum_{i \& j}^M P_i^j \ln (1/ P_i^j)$$

P_i^j = share of the segment i of group j in the total sales of the group.

3. Entropy measure of unrelated diversification can be calculated as:

$$RD = \sum_{j=1}^M P^j \ln (1/ P^j)$$

P^j = share of jth group sales in the total sales of the firm and

M = Number of industry groups where a firm is working.

Entropy measure requires segment sales data, segment description explaining the nature of product or services in each segment, and classification scheme for industry groups and industry segments along with their SIC (Standard Industrial Classification) codes. As it was previously stated that public listed companies in Malaysia are required to disclose their segment reporting data in their annual reports as per MFRS8 Operating Segments issued by MASB. This involves segment description about nature of products or services in each segment along with segment financial data including segment sales data. The data about

product segment sales is also available in Datastream. Therefore, for the purpose of this study, data sourced from annual reports as well as Datastream are verified for its accuracy.

SIC codes are used to differentiate among industry segments and industry groups. In case of a four digit SIC code, the difference in the first two digits represents different industries whereas the difference in the last two digits represents different segments in a particular industry. Chari et al. (2008) and Mehmood (2015) provide detail explanation on different components of entropy measure. As per their deliberations, related component of entropy measure (RD) measures the diversity of company's operations in different industry segments within the same two-digit SIC code. Whereas unrelated component of entropy measure (UD) measures diversity of company's operations in different two-digit SIC codes. Finally, total diversification (TD) measures the extent of company's operations in different industries whether they are related or unrelated. Total Diversification (DT) of a company is equal to sum of its related diversification (RD) and unrelated diversification (UD).

With regards to the entropy score calculations, this research uses Thomson Reuters Worldscope categorization of industry groups which is available on the basis of four (4) digits SIC codes. Since the SIC codes are not readymade for Malaysian PLCs. The, SIC codes are assigned manually to all segments (based on Worldscope categorization of industries) on the basis of segment description available in companies' annual reports. In view of this, if for any two segments, the initial two digits of their SIC codes are different, then the two segments belonged to different industries. However, in case it happen that the

two segments had same first two digits in their SIC codes but different last two digits in their SIC codes, then the two segments belonged to the same industry.

Precisely, the following procedure is adopted to calculate entropy scores for diversification:

i. Firstly, segment detail disclosed in the annual reports under MFRS8 Operating Segments are studied for every company to reveal the number of operating segments and their description.

ii. Secondly, Worldscope classification of industry groups are used to assign codes to segments based on their description.

iii. After that, segment external sales, assets and earnings data was used to calculate diversification scores using entropy formulae. Initially total diversification score is calculated, followed by related diversification score and unrelated diversification score. In the end, related and unrelated diversification scores are added to compare with the total diversification score as a cross verification.

3.6.9 Diversification Value

The performance of diversified companies is valued using the natural logarithm of 'excess value'. Excess value is measured by Berger and Ofek (1995)'s approach as adjusted by Lins and Servaes (2002) Claessens et al. (1998) and Fauver, Houston and Naranjo (2003), Akben Selcuk (2015) in an international context. The study of Ishak (2004) also adopted the approach.

The excess value for company is referred to as the natural logarithm of the ratio of the company's actual value to its imputed value. Actual value is measured as the company's total capital, that is, book value of debt plus market capital capitalization (market value of equity). While the imputed value is the sum of the imputed values of company's segments. The study calculated the imputed value of each segment by multiplying the median ratio, for single-segment firms in the same industry, of total capital to one of three accounting items (assets, sales, or earnings) by the segment's level of the accounting item. Each segment is determined by multiplying the three accounting items (sales, assets & earnings) allocated to that segment by the segment's industry median capital to each of the accounting item. Industry median ratio is constructed using single- segment companies.

The calculation of the excess value (Berger & Ofek, 1995; Ishak, 2004 approach) is summarized as in the following equations:

$$\text{ACTUAL} = V \quad (\text{i})$$

$$\text{IMPUTED} = \sum_{i=1}^n \text{TR}_i * [\text{Ind}_i (v/ \text{TR})_{\text{mc}}] \quad (\text{ii})$$

$$\text{EXCESSTR} = \text{Log} (\text{ACTUAL}/\text{IMPUTED}) \quad (\text{iii})$$

Where;

V = Total capital (book value of debt plus market capitalization) of the Company.

TR_i = Sales, Assets or earnings of segment *i*

$Ind_i (V/TR)_{mc}$ = Industry median, total capital to sales ratio (based on median multiple Segment i's industry).

n = Total number of both two – digit and four –digit segments i's company.

EXCESSTR=Natural logarithm of excess value using either of accounting items (sales, assets and earnings) multiplier.

Berger and Ofek, (1995) used three accounting items, that is, sales, assets, and earnings, as multipliers for calculating segments' imputed values. Claessens et al. (2001), Lins and Sarveas (2002); Fauver et al. (2003); Ishak (2004); Custodio, (2014); Ahuja and Novelli (2017) and Matvos, Seru & Silva, (2018) used only sales items because the Worldscope database used by them lacks segment assets and earnings. This study focus on the three accounting items (sales, assets & earnings). It is argued that the segment whose earnings may not be reliable because it is directly based on current profitability (Berger & Ofek, 1995). It is further argued that segment asset has a potential valuation problem related to differences between purchase and pooling accounting (Graham, Lemmon & Wolf, 2002). Custodio (2014) further address an important bias issue with respect to the calculation of imputed values based on assets (like Tobin's Q). Among others like Lee, Hooy and Hooy (2012) and Jiraporn, Kim, Davidson and Singh (2006) and Custodio (2014) recommends to use sales ratios to calculate imputed values because these are not (or less) affected. However, this study uses all the three accounting items in other to ascertain the individual effect on diversification value.

The validity of the multiplier approach depends on management disclosure policies (Berger & Ofek, 1995). Theoretical models of managerial disclosure decisions suggest that

managers may have incentives to misstate segment data to both providers of capital and product market competitors. Their ability to misstate depends on the discretion managers have to allocate resources between segments. Since segment assets must be specifically identifiable with the segment for which they are reported, there is little discretion to misstate them. Managers do have some ability to allocate sales and greater discretion to allocate expenses, so segment sales and earnings (sales less expenses) are vulnerable to manipulation. Givoly, Hayn, and D'Souza (1993) assess the quality of segment reporting, with quality defined as the difference between the correlation of accounting measures from segments with those of their industries and the correlation of measures from single-line firms in the same industries with the aggregate industry measures. They find a marginally significant difference in correlation coefficients of for sales and a significant difference of for earnings (Berger & Ofek, 1995). Thus, there is some evidence that the segment earnings numbers may not be as reliable as segment sales and asset figures. The earnings multiplier has the advantage, however, of imputing value directly from current profitability, which may be more directly linked to firm value than sales or assets. However, based on the above arguments on the choice of the most preferred accounting item to measure excess value. There is a need to undertake further study with all the three accounting items (sales, assets & earnings) to measure excess value, in order to ascertain the individual effect of each item on firm value.

3.6.10 Wealth Maximization

Corporate diversification to achieve manager's wealth maximization will serve the shareholders' at the same time (Li, 2007). Hence, based on the studies of Ueng and Wells (2001) and Li (2007) wealth maximization is defined by manager IR, which is measured

by dividing the market value of equity holdings of the three managers with the largest equity shareholder within their firm by their annual compensation. Huang and Hilary (2018) measured manager's wealth maximization with the log of total annual compensation of executive directors. Meanwhile, in line with the study of Huang and Hilary, this study measured manager's wealth maximization with the log of total annual compensation of executive directors.

3.7 Control Variables

In addition to examining the relationships between independent, dependent and moderating variables in the study, the analyses also controlled certain variables found by previous researches to be playing important role in the proposed relationships. Past studies controlled number of variables suitable to their purpose. Previous studies considered certain variables to be important in studying corporate board, diversification and performance relationship as they could also have an impact on corporate performance. Therefore, this study controlled those important variables namely size (Burgers, Padgett., Bourdeau, & Sun, 2009; Daud et al., 2009; Liu & Hsu, 2011; Marinelli, 2011; Shukla & Dwivedi, 2016), leverage (David et al., 2010; Marinelli, 2011; Chakrabarti et al., 2007; George, 2007; Liu & Hsu, 2011; Sharma, 2016) and firm age (Cheng, Chan, & Leung, 2010; Oh et al., 2015).

Company size is significant factor to be controlled as it is related to degree of market power a company enjoys and serves as a determinant of economies of scale benefits (Chari et al., 2008; Galván et al., 2007). Similarly, in diversification studies, it is important to control for leverage as it indicates company's financial structure, it's willingness to accept higher

risk and it might have profound impact on corporate performance (Hoechle et al., 2012). In the same way, a company's age is also a determinant of its success and failure and controlling for age controls for any experiential effects (Lange, Boivie, & Henderson, 2009; Liu & Hsu, 2011).



Table 3.2***Summary of Variables and Measurements***

Dependent Variable: (Financial Performance)	Notation	Measurement
<u>Dependent Variable:</u>		
Diversification Value		
	EVS	Excess Value: Natural log. of the ratio of actual to imputed value (using sales multiplier).
	EVA	Natural log. of the ratio of actual to imputed value (using assets multiplier).
	EVE	Natural log. of the ratio of actual to imputed value (using EBIT multiplier).
<u>Independent Variable. 1:</u>		
(Corporate Board)		
Tenure of an Independent Director	TIND	Total number of independent directors that serve a tenure of not more than 9 years.
Board Size	BSIZE	Total number of directors on the board.
Risk management committee	RMC	Binary variable coded as '1' if a risk management committee exists and as '0' if otherwise.
Board Independence	BIND	Proportion of independent directors in the board.
CEO Expertise	CEOEXP	Dummy variable "1" if CEO possesses a graduate level academic degree in any business and finance related field, "0" if otherwise.
Audit Committee Independence	AIND	Proportion of independent directors serving on the audit committee
Audit Committee Size	AUS	Total number of members in the audit committee.

Independent Variable. 2:

(Diversification Strategies)

Related

RD

Measures the diversity of company's operations with the same two-digit SIC code

Unrelated	UD	Measures diversity of company's operations in different two-digit SIC codes
Total Diversification Strategy	TD	Summation of related diversification (RD) and unrelated diversification (UD)

Moderating variables

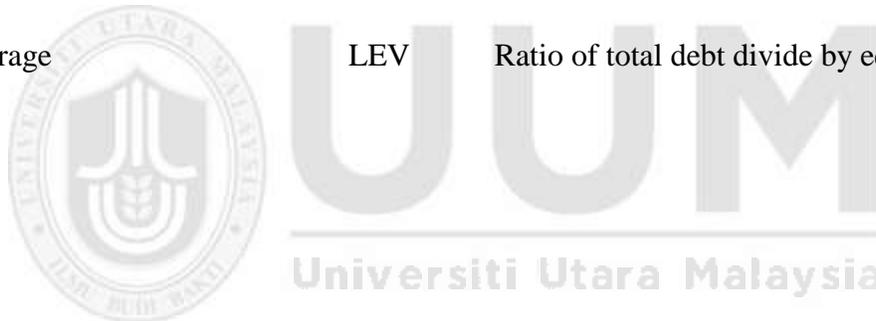
Managers' Wealth Maximization	MWM	Natural logarithm of Annual compensation of executive directors.
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Control Variables:

Corporate Size	CSIZE	Natural logarithm of book value of total asset.
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Corporate Age	CAGE	Number of years since establishment.
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Leverage	LEV	Ratio of total debt divide by equity.
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Corporate diversification strategies can differ significantly between companies, not only in the number of businesses in which each competes, but also in the nature of the relationships between those businesses. As alluded previously, certain scholars have noted that a firm can vary either in the level (extent) of diversification or in the nature (type) of diversification (related or unrelated). The level of a firm's diversification can be operationalized very simplistically by counting the number of businesses in which the firm operates. The more businesses in which a firm competes, the higher a level of diversification it is considered to have. More robust operationalization (e.g., the entropy or

concentric measure) of the extent of diversification are based on the distribution of the firm's revenue across its various businesses.

In order to clearly differentiate between the types of relationships among the businesses in a firm's portfolio, researchers need a means by which to define and categorize those relationships. In related diversification, the lines of business in a firm's portfolio are similar enough that resources and capabilities associated with technologies, production processes, distribution channels, and other elements can be shared among them. In contrast to related diversification, there is no underlying sharing of resources and capabilities between lines of business in a firm using an unrelated diversification strategy, although there may be a "parenting advantage", through which corporate-level core competencies are shared with the individual business units (Wiersema & Beck, 2017). This conceptual distinction between related and unrelated diversification is difficult to operationalize in practice, due in part to the limited availability of information and data regarding the firm's businesses and the extent to which their underlying resources and capabilities are shared.

Regarding the operationalization of diversification, continuous measures such as the concentric and entropy indices are the predominant means used to capture the firm's level of diversification, as well as the extent of the firm's related and/or unrelated diversification. These measures capture diversification utilizing the two-digit, three-digit, and four-digit Standard Industrial Classification (SIC) of the industries in which the firms operate. However, these are alternative approaches to measuring diversification (as well as conceptualizing "relatedness"), and "they can produce contradictory results because they differ in their sensitivity to underlying dimensions of portfolio strategy" (Adner & Zemsky, 2016).

3.8 Data Analyses Procedures and Techniques

Several statistical techniques can be used in analyzing the relationship between corporate board, diversification strategy and corporate value. Accordingly, the data were analyzed using descriptive and inferential statistics. Frequency count and percentage are used in descriptive statistics to define the research data, while the statistical tools of maximum, minimum, mean, standard deviation and variance are appropriate for measuring the central tendency. Correlation and multiple regressions are used for inferential statistics. The Pearson correlation is used to measure the significance of linear bivariate between variables (Babbie, 2004; Al-ebel, 2013). To determine the relationship between the independent, moderating and the dependent variables, and the direction, degree and strength of the relationship, interaction moderation effect is used.

3.8.1 Descriptive Statistics

The data was analyzed using descriptive and inferential statistics. Descriptive statistics for mean, standard deviation, maximum and minimum values were calculated for different variables.

3.8.2 Correlations

The study tested the relationship between the variables for his hypotheses. Pearson's correlation coefficients established the relationships among the variables (Zikmund, 2003; Babbie, 2004; Al-ebel, 2013). Pearson's correlation is used to see any relationship between the independent variables and the dependent variable. Through Pearson's correlation, the reader can identify whether there is any relationship between the variables. It shows the strength and direction of the relationship. However, as a rule of thumb, multicollinearity

may be a problem if a correlation is more than 0.90 or several are more than 0.70 in the correlation matrix formed by all the independent variables (Cohen & Cohen, 1998). Pearson correlation was used to determine the nature of relationship between all variables under study so as to understand their individual relationship with one another before regressing them. The value ranges from -1 to +1, but specifically there are four logic behind correlation coefficient which are:

- i. If the variables are independent i.e. there is no relationship between them the correlation coefficient is zero (0).
- ii. If the variables exhibit a perfect positive relationship i.e. +1 the variables are positively related, which means as one variable changes the other changes with the same proportion and direction.
- iii. If variables show a perfect negative relationship i.e. when correlation is equal to -1, it means as one variable increases the other decreases by the same proportion.
- iv. If correlation coefficient is between positive perfect relationship (+1) and a perfect negative (-1), the closeness of the direct or inverse relationship between the relationship of the variables determines the extent of their correlation.

3.8.3 Multiple Regression Techniques

The main advantage of multiple techniques is that they accommodate multiple variables in trying to understand complex relationships that are beyond the univariate and bivariate methods (Hair et al., 1998; Al-ebel, 2013). In an attempt to determine the variations in dependent variable (diversification value) due to variation in any of the independent variables (corporate governance and diversification strategies), the study used multiple

regression analysis. This is because multiple-regression is expected to explain the variation in dependent variable due to variation in any of the independent variables. However, the selection of the appropriate statistical techniques among the many multiple statistical tools that are available surely depend on the measurement of the research variables.

3.8.3.1 Meeting Assumptions for Multiple Regression Analysis

Multiple regression analysis combines together various independent variables to study their impact on a dependent variable (Kassim, 2013; Gujarati, 2006). There are usually various econometric problems associated with multiple regression. These problems need to be examined for ensuring that the interpretations of all regression models are valid. There are certain major assumptions of multiple regression, some of which are addressed in this research and are discussed in this section. These are; outliers, sample size adequacy, normality, linearity, homoscedasticity, autocorrelation, and multicollinearity.

3.8.4 Model of the Study

The multiple regression model technique was used to estimate the model of this study. In specific term, two regression models were set out in this study. Model 1 which contains both the independent variables and control variables was designed for regression estimating the main effect of the study and the result obtained from the model is utilized to validate hypotheses H1 to H11. While model 2 was set up to test the moderating effect of managers' wealth maximization. The models are presented in the form equation below:

$$\begin{aligned}
 \text{DV (EV)} = & \beta_0 + \beta_1 \text{BIND} + \beta_1 \text{AIND} + \beta_2 \text{CEOEXP} + \beta_3 \text{TIND} + \beta_4 \text{RMC} + \beta_6 \text{BS} + \beta_5 \text{ASIZE} \\
 & + \beta_7 \text{RD} + \beta_8 \text{UD} + \beta_9 \text{CSIZE} + \beta_{10} \text{AGE} + \beta_{11} \text{LEV} + \text{MWM}_{12} + e \dots \dots \dots (1)
 \end{aligned}$$

$$DV (EV) = \beta_1 RD * MWM + \beta_2 UD * MWM + \beta_3 BIND + \beta_4 AIND + \beta_5 CEOEXP + \beta_6 TIND + \beta_7 RMC + \beta_8 BS + \beta_9 CSIZE + \beta_{10} 12CAGE + \beta_{11} LEV + e \dots \dots \dots (2)$$

Where: β_0 , and $\beta_1 - \beta_{13}$ represent the intercept and regression coefficient respectively while $e =$ stands for the error term. DV which is the Diversification Value measured with excess value (EV).

Excess Value is measured using the three accounting items multipliers;

1. Sales multiplier
2. Assets multiplier
3. Earnings multiplier

BIND = Board Independence

CEOEXP = Board Expertize

AIND = Audit Committee Independence

TINDD = Tenure of independent Directors

RMC = Risk Management Committee

BS= Board Size

ASIZE= Audit Size

MWM= Managers Wealth Maximization

RD = Related Diversification

UD = Unrelated Diversification

CSIZE = Corporate Size

CAGE = Corporation Age; LEV = Leverage.

3.9 Chapter Summary

This chapter started by presenting research framework and listing research hypotheses. Then, it discussed population, unit of analysis and time period of the study. Detailed information was presented on the measurement of PLCs in Malaysia corporate governance (independent variable) diversification strategies (independent variable), managers' wealth maximization (moderating variable) and diversification value (dependent variable). The techniques and instrumentation for measuring different variables were discussed along with source data and instrument validation.



CHAPTER FOUR

ANALYSIS AND INTERPRETATION

4.1 Introduction

This chapter presents the analyses and discussions of the objectives of the study, which is the relationship between corporate governance, diversification strategies and diversification value. The chapter begins with explanations on the descriptive statistics. This is followed by discussions on basic assumptions for multiple regression analysis, moderating, explanatory and control variables. The next section presents the results and discussions on multiple regression results. The chapter further discusses the result of the moderating effects on the dependent variables. Lastly, the chapter presents results and discussions on the superiority of diversification strategies (related & unrelated).

4.2 Descriptive Statistics

Descriptive statistic is a quantitative measure for examining, summarizing and describing the relevant characteristics of collected data with the view to organize and display the data in a clear, logical, concise and meaningful manner Coakes and Steed (2007) as cited in Usman (2018). For the purpose of this study, the descriptive statistics of the independent, dependent and control variables are as depicted in their respective tables. Accordingly, the next section discusses the descriptive analyses of corporate board of the sampled companies.

As can be seen in Table 4.1, the mean, minimum and maximum of board size is 7.6, 4 and 17 respectively. This indicates that on average, 8 persons sit on the board of Malaysian firms with a minimum of 4 persons and maximum of 17 persons. This is similar to the size of Singaporean firms with average of 8 persons on the board with maximum and minimum of 13 and 4 persons respectively (Cheng & Courtenay, 2006). Comparatively, the average size of Malaysian boards is similar to the 7 persons obtainable in the UK (Guest, 2008), and differs with the 11 persons in Spain (Castro et al., 2009) and 13 persons in the USA (Hartarska & Nadolnyak, 2012). The average board size of Malaysian listed diversified companies is within the size recommended for achieving high level of board effectiveness by Lipton and Lorsch (1992) as cited in the study of Salina and Nazrul (2015), this is also supported by the studies of (Ishak 2004; Anum, 2010; Maigoshi, 2017). This finding supports the view that Malaysian listed companies have a preference maintaining a medium number of directors on the board. The code states that the board should examine its own size, with a view to determining the impact of the number upon its effectiveness.

In terms of board independence, the descriptive statistic indicates that the Malaysian listed companies complied with the recommendations of the code on corporate governance to have at least one third of the board comprising independent directors. The result show that the mean of the board independence is around 44% and the standard deviation of 11%, for the variable is not much volatile. On average, the mean of the board independence is above the one-third requirement of MCCG (2007). The minimum value of 20% for the board independence indicates that there still exist some firms that are yet to meet the requirement of at least one-third for independent directors.

On the other hand, 68% of the independent directors served a cumulative tenure of less than nine years. This is in line with the requirement of the MCCG (2017) that independent directors of Malaysian PLCs are requisite to serve for a cumulative term of nine years. Upon completion of the nine years, an independent director may continue to serve on the board subject to the director's re-designation as a non-independent director.

The mean of the audit committee independence is 0.65 indicating that independent directors dominate the membership of the audit committee in most of the Malaysian listed diversified firms. This is consistent with the requirement of MCCG (2017) that independent directors should constitute the majority of audit committee members. The result is also in line with the study of Wan-Hussin (2009) and Maigoshi (2017). The size of the audit committee has a minimum 3 members and a maximum of 6 members. This is in line with the study of Kipkoech and Rono (2016) and Anderson et al. (2012) who suggests that the audit committee be composed of three or more directors. The Cadbury Report (1992) and the Smith Report (2003) stipulate the number of audit committee members must be at least three; the Sarbanes–Oxley Act (2002) also mandates a minimum of three members in the audit committee.

Buchalter and Yokomoto (2003) recommend that audit committees should be composed of three to five members although it is generally based on the firm's size, implying that the size of the audit committee is indicative of its ability to fulfill its governance obligations. The MCCG (2012) recommends that there should be at least three non-executive directors in the audit committee, a majority of whom should be independent. The mean of CEO

expertise is 60% indicating that more than half of the CEOs of the sampled PLCs are financially literate. This is consistent with the study of Maigoshi (2017).

The risk management committee has a mean of 63% which shows that more 60% of the sampled firms reported the composition of their risk management committee members this is similar to what was obtained in the study of Ong et al. (2015). However, Malaysian companies without a stand-alone risk management committee report that the oversight of their risk management and control activities is embedded in the internal audit functions (IAF) which report to their audit committees on the state of their internal controls (Yatim, 2010). A survey of 380 publicly listed Malaysian firms by the Institute of Internal Auditors Malaysia also reveals that 58 percent of these firms have their own internal audit function (IAF) (IIA Malaysia 2003). The result shows that a minimum of RM153, 000,000 and a maximum of RM16, 602,000,000 was paid as annual compensation to the managers of the listed diversified PLCs in Malaysia.

The descriptive result further shows that total diversification strategies have a mean of 0.65, indicating that 65% of the diversified companies engaged in both diversification strategies (related and unrelated), that is, the 65% adopt both strategies at same time. In addition, based on the mean value of the two diversification strategies, the value of unrelated strategy has a mean of 0.35 which is greater than the related diversification with a mean of 0.30, this indicates that 35% of the diversified companies engaged in unrelated diversification strategy and 30% adopted the related strategy. Thus, it shows that the level of the unrelated diversification strategy by the listed PLCs in Malaysia is slightly higher than that of the related diversification strategy.

The mean, standard deviation, minimum and maximum of corporate size is 12.82, 8.68, 11.08 and 14.83 respectively. The difference between the mean and standard deviation of the firm size indicates that there no substantial variation and the variable is normally distributed. The average mean of leverage is 0.44 which indicates that the average leverage of the diversified firms is 44%. The descriptive results show that the maximum age of incorporation of the listed diversified firms in Malaysia is 98 years.

The natural log of the ratio of a firm's actual value to its imputed value is the measure of excess value. The study calculated the imputed value of each segment by multiplying the median ratio, for multiple-segment firms in the same industry, of total capital to one of three accounting items (assets, sales, or earnings) by the segment's level of the accounting item. As can be seen from the result, the sales multipliers has the highest mean of 3.59, which is in line with the study of Ishak (2004). Jiraporn, Kim, Davidson and Singh (2006) and Custodio (2014) recommends the use of sales multiplier to calculate imputed values because it have more effect on firm value and are not vulnerable to manipulations. The asset multiplier has the second largest mean with 2.45. The use of this multiplier for the valuation of excess value is supported by the study of (Berger & Ofek, 1995). Although, the earnings has the lowest mean of 2.25, but it was also supported by the study of Berger and Ofek (1995), that the earnings multiplier has the advantage, however, of imputing value directly from current profitability, which may be more directly linked to firm value than sales or assets multipliers.

Table: 4.1
Descriptive Statistics

Variable	Mean	Std. Dev.	Min	Max
BSIZE	7.56	2.01	4	17
BIND	0.44	0.11	0.2	1
AIND	0.65	0.20	0.20	0.90
ASIZE	3.33	0.59	3	6
CEOEXP	0.60	0.48	0	1
RMC	0.63	0.48	0	1
TIND	0.68	0.45	2	4
MWM	1,123.12	4,342.1	153	16,602
TD	0.65	0.34	0.01	1.69
RD	0.30	0.31	0	1.33
UD	0.35	0.31	0	1.47
CAGE	31.60	13.94	3	98
CSIZE	12.80	8.66	11.08	14.83
LEV	0.44	0.12	0.13	1
EVS	3.59	0.61	3.16	4.83
EVA	2.45	0.53	2.32	3.66
EVE	2.25	0.50	2.69	4.03

BSIZE= Board size; BIND=Board independent; AIND=Audit committee independent; ASIZE= Audit committee size; CEOEXP= CEO expertise; RMC=Risk management committee; TIND=Tenure of independent directors; MWM= Managers' Wealth Maximization; TD= Total diversification; RD= Related diversification; UD= Unrelated diversification; CAGE= Corporate age; CSIZE= Corporate size; EVS= Excess value (using sales multiplier); EVA= Excess value (using asset multiplier); EVE= Excess value (using ebit multiplier)

4.3 Multiple Regression

This section presents the results of the diagnostic tests conducted to ensure that the data used by the study satisfied all the basic regression assumptions. The section also contains the results of the model specification tests to ensure that the research models are correctly specified, as well as model selection criteria and with the presentation and discussion of the results of the estimation models.

4.3.1 Meeting Assumptions for Multiple Regression Analysis

Multiple regression analysis combines together various independent variables to study their impact on a dependent variable (Gujarati, 2006; Azlina, 2013). There are usually various econometric assumptions associated with multiple regression. These problems need to be examined for ensuring that the interpretations of all regression models are valid. There are seven major assumptions of multiple regression (Mehmood, 2015) which are addressed in this research and are discussed in this section. These are; sample size adequacy, outliers, normality, linearity, homoscedasticity, autocorrelation, and multicollinearity. The study conducts the Doornik and Hansen (2008) normality test, Breusch and Pagan (1980) heteroskedasticity test, Hair, Babin and Anderson (2014) variance inflation test of multicollinearity and Pregibon (1980) model specification test and finally, the study employs Dixon (1980) outlier treatment method to minimize the effect on regression coefficient estimates. The examination of these regression assumptions reveals that all assumptions were met.

Table 4.2

Result of Diagnostic Tests

<u>Test</u>	<u>P-Value</u>
Test of Normality (Doornik-Hansen)	0.1004
Heteroskedasticity (Breusch & Pagan)	0.1132
Test for Multicollinearity (VIF Test)	1.77
Model specification test (Hat test)	0.3054
Model specification (Hat –square)	0.4761

4.4 Sample Size Adequacy

In this study, the unit of analysis is a diversified listed PLC(s). As shown above, 490 companies were included in the analyses after data cleaning and screening. In determining the appropriate sample size, suggestions put forwarded by Sekaran (2013) and Coakes, Steed, and Price (2008) are followed in line with Azlina (2013) and Mehmood (2015). The first opinion suggested that, in a regression analysis, the sample size should be ten times the number of variables used by the study (Coakes, Steed & Price, 2008). While the contrary view argues that the minimum sample size must be five times the number of variables used by the study (Sekaran, 2013). In this study, the number of variables included in a model is fourteen (14) as explained in the previous chapter. Hence, a sample of at least 140 (10x14) companies was required and the minimum sample size should be 70 (5x14). In line with the above discussions, the sample size of 490 was deemed fit and considered appropriate for analyses.

4.4.1 Outliers

Outliers are observations with unique attributes that differ from the other observations (Hair et al., 2014). To uphold the assumption of treating the outlier variables, all the continues variables with unusual observations can either be winsorized at 1% top bottom (Maigoshi, 2017). According to Kubota, Suda and Takehara (2011), as well as Mechelli and Cimini (2014), the data should be winsorized at 2% in order to solve the issue of outliers. Dixon (1980) states that winsorization of data gives more stable results than trimmed means. Hence, this study winsorized the unusual variables at 2%.

4.4.2 Normality Test

Normality test is vital in numerous statistical methods. When this postulation is violated, analysis and inference may not be reliable and or valid (Park, 2015). The regression model is fit based on the assumptions that the residuals follow a normal distribution. Normality, being the fundamental assumption in data analysis, refers to the shape of the data distribution for an individual metric variable and its correspondence to the normal distribution. Hair et al. (2006) term it as the benchmark for statistical methods. Since it has become a requirement to use the F and t statistic, the variation from the normal distribution needs to be small. Large variations renders all statistical tests resulting from the analysis invalid (Al-ebel, 2013). There are several ways in which one could describe the distribution of the data if it differs from the normal distribution.

This study used Doornik and Hansen (2008) multivariate normality test in order to test the normal distribution of the residual of the model. The p-value of 0.1004 as presented in Table 4.2 indicates that the residual of the model is normally distributed. A graphical method of normality test was also employed in order to support the results of the Doornik-Hansen test for multivariate normality. The histogram and density normal test was performed to check the pictorial distribution of the data. The regression model is fit based on the assumptions that the residuals follow a normal distribution. Figure 4.1 evidently shows a normally distributed histogram curve. The curve is neither skewed left nor to the right side of the plot displaying a bell shape. Similarly, the pattern of all the bars on the histogram is close to normal. Hence, normality distribution is strictly adhered to. Meanwhile, Figure 4.2 shows the normality P-Plot graph with an approximate straight line that is close to the fitted

line. This indicates that the variables are in a form of normal distribution. Therefore, following these procedure, normality assumption is not violated in this study.

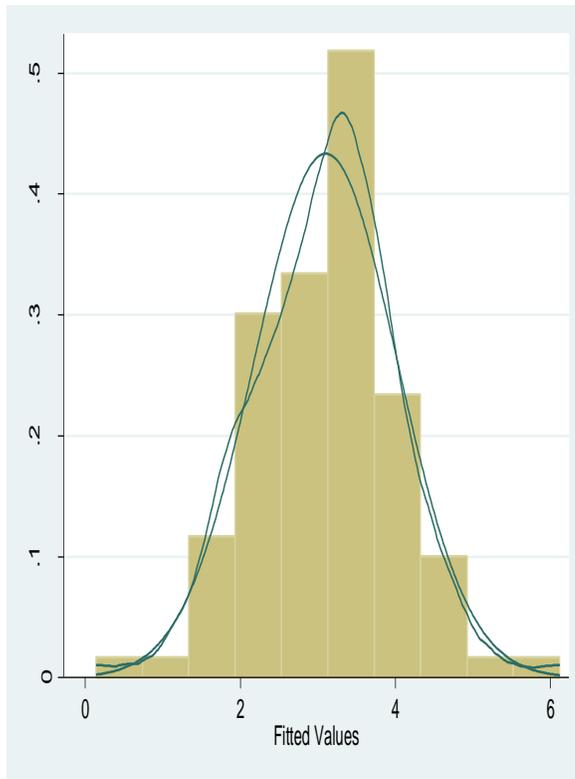


Figure 4.1: Histogram Normality

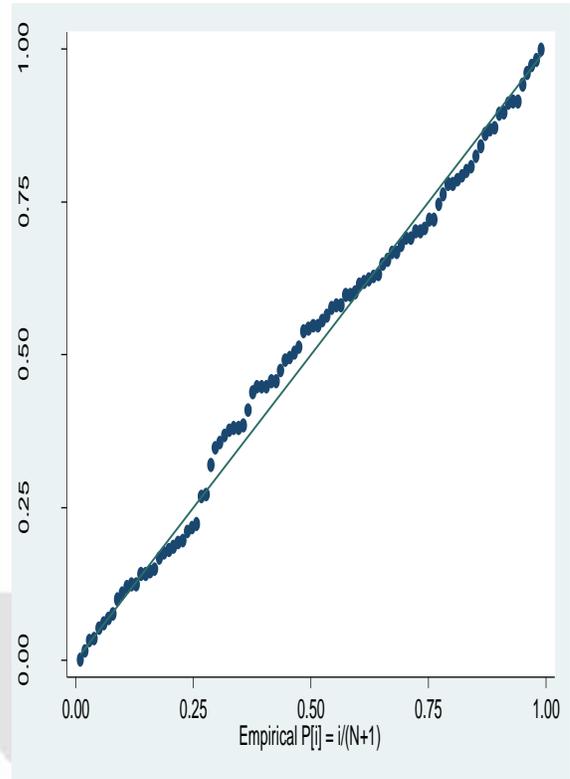


Figure 4.2: P- Plot Graph Normality

4.4.3 Heteroskedasticity

Breusch-Pagan/Cook-Weisberg test for hetetroskedasticity was used in this study to test for the homoscedasticity of the regression model. The p-value of 0.1132 in the Breusch – Pagan/Cook-Weisberg test for hetetroskedasticity as presented in Table 4.2 shows that the model is homoscedastic. A graphical residual versus fitted value (RVF) plot was used to support the result of the Breusch-Pagan/Cook-Weisberg test for hetetroskedasticity. Figure 4.3 graphs the residuals against the fitted values which shows that the dots seem to fluctuate around zero in an unpattern direction, hence, indicating that the model used in this study is homoscedastic.

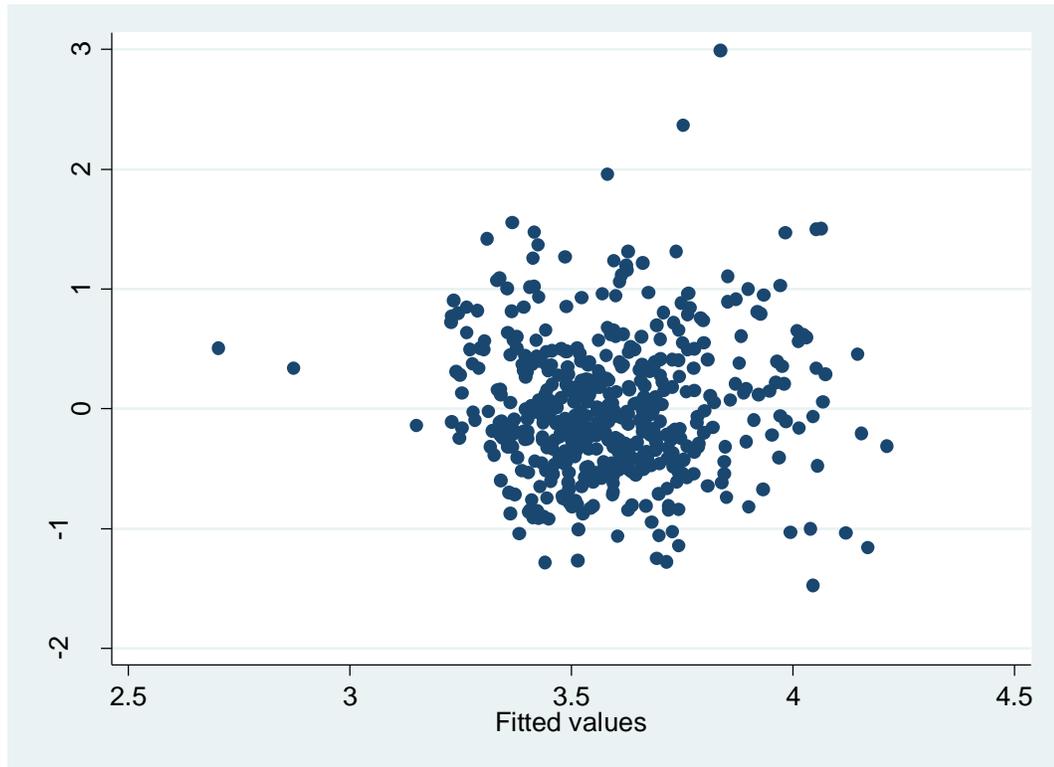


Figure 4.3: Residual versus Fitted Value Plots

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4.4.4 Linearity

The relationship between the dependent variable and independent variables are test for linearity. The linearity assumption provides that the relationship between dependent and independent variables should be linearly distributed. The linearity between dependent and independent variables demonstrates the degree to which changes in the independent variable affects the dependent variable. In this study, the linearity relationship is tested by comparing the standard deviation of the dependent variable with that of the residual of regression (Maigoshi, 2017). The rule of thumb is that linearity is achieved if the standard deviation of the dependent variable is greater than that of the residual of the model (Garson,

2012; Hair et al., 2014). Table 4.3 presents the standard deviation of the dependent variable and the residual of regression. It reveals that the standard deviation of the dependent variable is greater than that of the residual. Hence the linearity assumption is satisfied.

Table 4.3
The Standard deviation of firm value and Residual

Variable	Standard Deviation
Firm Value	0.4659
Residual	0.3054

4.4.5 Multicollinearity

Before the regression results are considered valid, the degree of multicollinearity and effect on the results are examined. Multicollinearity is the inter-correlation of independent variables. Multicollinearity decreases the ability to predict the measure and ascertain the relative role of each independent variable. Substantial multicollinearity between independent variables is not good as the estimated regression coefficient becomes unreliable. To check for multicollinearity, this study looks at the correlation matrix (r) for the univariate analyses between independent variables and the variance inflation factor (VIF). As a rule of thumb, multicollinearity may be a problem if a correlation is more 0.70 in the correlation matrix formed by all the independent variables (Cohen & Cohen, 1998). According to Hair et al. (2006), acceptable values for collinearity are considered from the tolerance value of more than 0.1 or the VIFs value of less 10 to indicate little or no multicollinearity. Furthermore, a maximum VIF value in excess of 10 is often taken as an indication that multicollinearity may influence the least squares estimates (Al-ebel, 2013). Accordingly, a large VIF value and small tolerance value indicates that there is a multicollinearity problem.

Table 4.4 presents the correlation matrix for the dependent, independent and control variables. The correlation coefficients between variables are obtained from Pearson tests. Overall, there are a number of statistically significant correlation between corporate boards, diversification strategies, firm value and control variables, the correlation is not more than 0.70. Thus, the results shown in Table. 4.4 indicates that there is no multicollinearity problem. The results of the standard test on VIFs in Table 4.5 also indicate that there is no multicollinearity problem, as the VIFs are below the threshold value of 10.

4.4.6 Univariate Analysis

As explained in previous chapter, correlation inferential statistical measurement between the dependent and independent variables was part of the approaches considered for this study. Correlation analysis is performed basically to determine the strength and direction of the relationship between observed variables (Pallant, 2011).

Table 4.4 presents the correlation matrix for the research variables. Generally, the results reveals non-existence multicollinearity problem among the research variables. The highest correlation among the research variables is 0.85 between leverage (LEV) and corporate size (CSIZE). This indicates a strong correlation exist between leverage and corporate size. The strength of the relationship between variables is interpreted based on the criteria popularized by Cohen (1988), that correlation value between 0.1 to 0.29 is small, 0.3 to 0.49 medium and 0.5 to 1.0 is large and harmful. Gujarati (2003) considers a correlation of more than 0.5 as high correlation. However, Hair et al. (2014) and Tabachnik and Fidell (2007) states that a correlation of more than 90% could not be a problem to estimation. Following Hair et al. (2014) and Tabachnick and Fidell (2007). Hence, the correlation

between leverage and corporate size, and the other explanatory variables in this case, does not expose the regression model to severe multicollinearity problem. Further, the study checked the variance inflation factors (VIF) for the regression analysis in Table 4.4, and find that multicollinearity is not a major concern. Multicollinearity is said to exist where the tolerance value is less than 0.01 and the VIF is more than 10 (Field, 2009; Al-ebel; 2013; Xie, 2014; Maigoshi, 2017). The accepted variables were therefore determined not to exhibit multicollinearity and suitable for collection and analysis.



Table: 4.4**Pearson Correlation Matrix of the Research Variables**

	EVS	EVA	EVE	BSIZE	BI	AIND	ASIZE	CEXP	RMC	TIND	MWM
EVS	1.00										
EVA	0.34	1.00									
EVE	0.32	0.54	1.00								
BSIZE	-0.11**	-0.27**	-0.29*	1.00							
BI	0.25***	0.16**	0.22*	0.52**	1.00						
AIND	-0.50***	-0.11*	0.20**	0.02	0.05	1.00					
ASIZE	-0.16*	-0.15***	-0.16**	0.23***	0.11**	0.26	1.00				
CEXP	0.05	0.03	0.06	0.22*	0.30***	0.51	0.67	1.00			
RMC	0.11*	0.18*	0.11**	0.01	0.08*	0.18**	0.16	0.14	1.00		
TIND	0.31*	0.17***	0.11**	0.15	0.07	0.06	0.01	0.08	0.06	1.00	
MWM	0.10**	0.24***	0.36*	0.22***	0.10*	0.00	0.13**	0.05	0.03	0.15	1.00
RD	0.25*	0.31*	0.01**	0.01	0.04	0.01	0.01	0.02	0.02	0.05	0.16*
UD	-0.04	-0.03	-0.05	0.04	0.03	0.13**	0.04*	0.04	0.04	0.06	0.12*
CAGE	0.01	-0.00	-0.06	0.02*	0.05**	0.01	0.31	0.21	0.11	0.15	0.24**
CSIZE	0.28***	0.55*	0.81**	0.37***	0.11**	0.02	0.27	0.35*	0.31***	0.18	0.39***
LEV	0.20***	0.50***	0.70***	0.28***	0.12**	0.03	0.21***	0.05	0.32***	0.15	0.36***

EVS= Excess value (Sales); EVA= Excess value (Asset); EVE= Excess value (Ebit); BSIZE= Board size; RMC=Risk management committee; MWM= Mangers Wealth Maximization; TD= Total diversification; RD= Related diversification; UD= Unrelated diversification; CAGE= Corporate age; CSIZE= Corporate size; *,**,*** Indicates that the parameter estimates are statistically significance at the 1%, 5%, and 10% levels respectively.

Table 4.4 (Continued)

	RD	UD	CAGE	CSIZE	LEV
RD	0.03				
UD	0.01	1.00			
CAGE	0.04	0.55***	1.00		
CSIZE	0.01	0.03	0.01	1.00	
LEV	0.02	0.28***	0.02*	0.85***	1.00

EVS= Excess value (Sales); EVA= Excess value (Asset); EVE= Excess value (Ebit); BSIZE= Board size; RMC=Risk management committee; MWM= Mangers Wealth Maximization; TD= Total diversification; RD= Related diversification; UD= Unrelated diversification; CAGE= Corporate age; CSIZE= Corporate size; *,**,*** Indicates that the parameter estimates are statistically significance at the 1%, 5%, and 10% levels respectively.



Table 4.5 shows that there is no evidence of multicollinearity problem as both the tolerance value and VIF are within the acceptable region. Hence, the accepted variables are considered suitable for collection and analysis.

Table 4.5
Collinearity Statistics; Tolerance Value (TV) and Variance Inflation Factor (VIF)

Variables	Collinearity Statistics	
	VIF	T V
BS	4.02	0.24
RMC	3.6	0.26
TIND	2.24	0.45
BI	1.77	0.56
CEXP	1.58	0.62
AIND	1.47	0.67
ASIZE	1.40	0.70
MWM	1.21	0.83
RD	1.21	0.83
UD	1.19	0.84
CAGE	1.14	0.88
CSIZE	1.05	0.95
LEV	1.02	0.98
Mean VIF	1.77	

Note. The mean VIF= 1.77; Where BS= Board size; RMC=Risk management committee; TIND=Tenure of independent directors; BI=Board independent; AIND=Audit committee independent; AUS= Audit Size; CEXP= CEO expertise; MWM= Managers' Wealth Maximization; RD= Related diversification; UD= Unrelated diversification; CAGE= Corporate age; CSIZE= Corporate size

4.4.7 Model Specification Test

Model specification bias may be as a result of a combination of omission of important variable(s), measurement error, and adoption of wrong functional form and or wrong specification of the stochastic error terms (Gujarati, 2004). This study employed the use of Pregibon (1980) model specification test in order to ensure the appropriateness of the study model. The results of the specification test as presented in Table 4.2 reveals that the p-

value of the Hat-square was 0.4761. This indicates that the research model is properly specify.

4.5 Regression Analysis Results

4.5.1 Relationship between Governance Mechanism Diversification Strategies and Diversification Value

Table 4.6 comprises of three different models which presents the coefficients of the regression for the determinant of firm value Model 1 represents the determinant of diversification value using excess value sales (EVS) multiplier, Model 2 presents the determinant of diversification value using excess value assets (EVA) multiplier and Model 3 shows the determinant with excess value EBIT (EVE) multiplier. Board size and board independent are components of corporate board adopted in this study to measure their influence on the value of listed diversified companies. The firm value was measured with three multipliers of excess value (sales, assets & EBIT). Board size is measured as the actual number of persons that sit on the corporate board.

It is widely believed that board size affects firm's value (Upadhyay, Bhargava & Faircloth, 2013). The benefit of shared responsibilities permits board members to go deep into financial reports and ensure that they comply with the requirements of relevant laws (Maigoshi, 2017). Based on this, it is hypothesized that board size improved the value of firms because of the diverse knowledge, skills and experience that are present on the large boards. However, the results from this study as presented in Table 4.6 do not support hypothesis one (H1) which presumed that board size have positive relationship with diversification value. Therefore, this confirms the accomplishment of the objective of the

study on the relationship between corporate board mechanisms and the diversification value of public listed companies in Malaysia. The coefficient of board size was negative in and significance at 5%, 5% and 10% for model 1, model 2 and model 3 respectively. That is, the board size maintains a negative relationship with diversification value in all the three multipliers of sales, Ebit and assets. The possible explanation for the negative relationship is the dominance of family members and cronies on the board (Maigoshi, 2017). In addition, when there are too many directors, it may become ineffective and inefficient.

Several empirical studies found a negative relationship between board size and firm performance, in developed countries such as the USA (Lehn et al., 2009), UK (Bennedsen et al., 2008; Guest, 2009), and in emerging Asian economies such as Singapore and Malaysia (Mak & Kusnadi, 2005; Shukeri et al., 2012), Thailand (Glaewketgarn, 2013), China (Liang et al., 2013) and Pakistan (Yasser et al., 2017), as well as in emerging economies in Africa like the case for banks in Kenya (Chepkosgei, 2013), and firms in Nigeria (Uadiale, 2010; Ugwoke et al., 2013). These findings support the explanations from agency theory (Harris & Raviv, 2006), about highlighting the importance of small boards to monitoring and controlling corporate management. One common interpretation of a negative board size and performance relation is that many boards are inefficiently and persistently too large, and that a 'one size fits all' approach to board size would improve performance for such firms (Jensen, 2010). According to Pfeffer (1972), board size depends on the conditions of the environment. Specifically, the conditions of economic volatility and uncertainty experienced in developing countries may lead to boards with a greater number of members to establish more and better relationships with other organizations and the environment, and to provide valuable resources for better firm

performance. Cheng (2008) suggest that larger boards exist even though they are value reducing, because they are necessary for some type of companies and under certain conditions.

On the other hand, board independent represents the proportion of independent directors on the corporate board. The coefficient of board independence in this study was positive and significance at 1%, 5% and 10% in model 1, model 2 and model 3 respectively. This indicates that there is a positive relationship between board independence and diversification value. The results support hypothesis two (H2) of this current study. Which presumed that, the board independent has a positive relationship with the diversification value. Hence, this confirms the achievement of the objective of the study on the relationship between corporate board mechanisms and the diversification value of public listed companies in Malaysia. This supports the agency theory which suggest that the presence of independent directors on the board minimizes agency problems (Adams, Hermalin, & Weisbach, 2008; Crespi-Cladera & Pascual-Fuster, 2014). This is consistent with the findings of previous studies which established that board independence enhances firm value (Ameer, Ramli & Zakaria, 2009; Cybinski & Windsor 2013; Liu, Miletkov, Wei & Yang, 2015).

Another aspect of internal governance mechanisms considered in this study is the audit committee characteristics. Audit committee independence and audit committee size were used in this study. To ensure the independence of audit committee, MCGG (2007) requires that independent directors should constitute the majority of audit committee members. This is due to the revelations by prior studies that the adequacy of independent directors protects

the interest of all shareholders (Lo et al., 2010; Mallin et al., 2016). However, contrary to the expectation, the coefficient of audit committee independence was negative and significance at 1%, 10% and 5% for model 1, model 2 and model 3 respectively. The result does not support hypothesis three (H3) of this study which assumed that the audit committee independence has a positive relationship with the diversification value. It is likely that the independent directors in the audit committee may have connections with the CEOs. This may impair their independence and thus, reduce their monitoring ability in the financial reporting process. This is because CEOs connection with the audit committee reduced the effectiveness of the committee in Nigerian firms (Sanda, Garba & Mikailu, 2011).

In addition to the possible explanations for this finding may be as a result of the issue of expertise (the combination of education and experience) of the independent directors. An independent member of audit committee without relevant experience and educational qualifications (i.e. qualified accountant or another finance professional with experience of financial and accounting matters) and proper understanding of the firm's industry may have little to contribute to the committee once it comes to reporting, monitoring and curtailing financial issues. In this case, the non- independence non- executive director with the required expertise may contribute to the effectiveness of the committee more than the presence of independent director without such expertise (Aldamen et al., 2012; Maigoshi, 2017). Greater independent director experience and audit knowledge results in more reliable reports (Aldamen et al., 2012)

The second variable under the audit committee characteristics is audit committee size. The regression result shows that the audit committee size maintains a negative and significant relationship with firm value at 10%, 1% and 5% for model 1, model 2 and model 3 respectively. This indicates that the size of audit committee members are negatively impacting on the value of listed diversified firms in Malaysia. Though, the coefficient was negative, it was statistically significant at all levels. The result does not support hypothesis four (H4) of this study which assumed that the audit committee size has a positive relationship with the diversification value. Consequently, the result produces a basis for rejecting the hypothesis formulated which presumed that audit committee size has positive significant effect on firm value of listed diversified companies in Malaysia. This is in line with the findings of Yang and Krishnan (2005) who also documented that audit committee size is negatively and significantly associated with firm value. It is also consistent with the findings of Lin et al. (2006) and Fodio et al (2013). The implication of this result is that, larger audit committees are better at reducing firm value (Bala & Kumai, 2015). This is as a result of many audit committee members been confronted with the problem of not having the necessary skills, knowledge and experience to act as audit committee members and perform their duties optimally (Kipkoech, 2016). This can also be explained by the increase in the professional fees of the Audit Committee (Aldamen et al., 2012; Bouaine & Hrichi, 2019).

The agency theory states that the presence of an audit committee within the board of directors is sufficient to ensure the reliability of financial statements. However, Beasley (1996) concluded that the mere presence of an audit committee does not necessarily mean that this committee is effective in performing its oversight role. Anderson et al. (2004)

argues that if the size of a team is large, individual members may be more vulnerable to the pressures and more subject to follow the others' opinion without giving another argument. In this case, the audit committee members are not likely willing to question the potential errors in the accounting reports of the internal review process, which in turn can lead to a greater chance of presenting again later. Conversely a small team will facilitate the exchange of information in the firm and a better discussion between members, to assist management to identify potential errors in financial reporting and reduce the incidence of restatement of the minimum size requirements. A large committee may suffer from the problem of free riders.



Table 4.6: Regression Result on the Relationship between Corporate Board, Diversification Strategies and Diversification Value

Variables	EVS Coefficient (t-value)	EVA Coefficient (t-value)	EVE Coefficient (t-value)
Board Size	-0.07** (-3.67)	-0.11** (-4.31)	-0.05* (-2.41)
BI	0.55*** (5.35)	0.16** (3.94)	0.25* (1.87)
AIND	0.03*** (-2.55)	0.02* (-1.76)	0.02** (-2.24)
ASIZE	0.03* (-2.09)	0.06*** (-3.54)	0.02** (-2.21)
CEXP	0.03 (0.07)	0.02 (0.06)	0.05 (0.07)
RMC	0.05* (2.41)	0.28* (1.89)	0.36** (3.69)
TIND	0.08* (-2.13)	0.07*** (-3.90)	0.03** (-2.71)
MWM	0.15** (3.29)	0.23*** (6.19)	0.07* (2.45)
RD	0.04* (2.06)	0.03* (2.05)	0.38** (3.71)
UD	0.04 (-1.00)	0.01 (-0.41)	0.03 (-0.33)
CAGE	0.03 (0.33)	0.03 (0.75)	0.01 (0.38)
CSIZE	0.02*** (9.91)	0.06** (2.54)	0.02** (3.52)
LEV	0.03* (1.87)	0.02* (1.86)	0.02* (1.85)
F-stat	0.00***	0.00***	0.00***
Adj. R-squared	0.29	0.29	0.33
Observation	490	490	490

Where BS= Board size; BI=Board independent; AIND=Audit committee independent; ASIZE= Audit Size; CEXP= CEO expertise; RMC=Risk management committee; TIND=Tenure of independent directors; MWM= Managers' Wealth Maximization; RD= Related diversification; UD= Unrelated diversification; CAGE= Corporate age; CSIZE= Corporate size; EVS= Excess Value Sales; EVA= Excess Value Asset; EVE= Excess Value Ebit *, **, *** Indicates that the parameter estimates are statistically significance at the 1%, 5%, and 10% levels respectively.

The next category of governance mechanisms in this study is the CEO financial expertise. A CEO with financial expertise is more likely to pilot the financial affairs of the firm effectively (Custodio & Metzger, 2013). The evidence of financial experts on the boards of directors or in the form of CEOs largely points to operational and financial improvements, efficiency gains, and better access to funding, mitigation of information asymmetry as well as increased investor confidence in the business. One should, however, be wary of the potential downside risks of such appointments, as they increase the risk-taking capacity of companies, or some of the biases described by behavioral finance theories, which could deteriorate the company's position, especially during crisis years.

Custodio and Metzger (2014) opined that the presence of directors with a career background in finance leads to more financially sophisticated policies and the ability to find better financing options for the companies even under adverse circumstances, thus making value-enhancing decisions on behalf of the shareholders. Such directors are able to overcome the weighted average cost of capital fallacy, where they distinguish between firm-wide and investment-specific weighted average. The companies they govern also hold less cash, more debt and engage in more share repurchases, overall pointing to a more dynamic style of management, responding faster to policy changes, such as dividend tax rate cuts. Similarly, Harris and Raviv (2008) argue in favor of the benefits of financial expertise within a company, stating that such skills decrease the costs of acquiring subject-specific information, recognizing and assessing the risks and complexity of the business model and environment and allow for better management and monitoring of a company.

Though the coefficient of the CEO financial expertise is positive as predicted, it is not statistically significant in model 1, model 2 and model 3 respectively. The result support hypothesis five (H5) of this study which assumed that the CEO financial expertise has a positive relationship with the diversification value. The possible reason may be as a result of concentrated ownership structure of firms in Malaysia. The appointment of severally financial expert CEO was influenced by the extent of their ownership and family decisions (Maigoshi, 2017). The studies of Chen et al. (2013) and Ansari et al. (2014) prove the influence of the family members on firm's practices. When the CEO is appointed from within the family, the family members enjoy from related monetary and non- monetary benefits from the firm and might hesitate to replace him regardless of the consequences of his decisions. Therefore, the family CEO provide opaque information to hide the rent-seeking activities of the family members and cover his under-performance (Maigoshi, 2017). Malmendier and Tate (2008) also draw the link between managerial overconfidence and their perceived ability to generate abnormal returns and conduct more acquisitions, which are value destroying on average.

The next variable is the risk management committee, risk management is an important element of corporate governance because it provides a means of realizing corporate objectives and monitoring the performance of an agent by a principal (McNutt & Demidenko, 2010). From an agency theory perspective, the purpose of the committee is to act on behalf of shareholders in assisting firms to understand and manage risk (Hassan, Mohd Saleh, Yatim & Rahman, 2012). The coefficient of the result shows that setting risk management committee have a positive and significant effect on diversification value for model 1, model 2 and model 3 respectively. The finding is in line with the study of Gates,

Nicolas and Walker (2012) and Aebi, Sabato and Schmid (2012). The result supports the earlier predicted hypothesis (H6) of the study.

Consistent with a risk-based approach, a board that puts in place firm-wide risk management system increases risk awareness within a firm. This increase in awareness and knowledge allows the board for more sound decision making and creates a positive impact on the governance structures and on control environment of the firm (Yatim, 2010). Auditors are likely to perceive boards of directors that actively participate in risk management as more thorough when reviewing the effectiveness of internal controls. This, in turn, reduces the likelihood that uncontrolled business risks cause unexpected losses, reputational damage or strategic setbacks. Further, firms that are proactive in risk management activities are not only able to detect and prevent frauds but can also enhance their financial reporting quality (Yatim, 2010).

The tenure of independent directors is one of the corporate governance variable used in this study. The study hypothesized a positive relationship between tenure of independent directors with diversification value. Though the outcome of the study is significant at 10%, 1% and 5% for model 1, model 2 and model 3 respectively, nonetheless, with negative coefficients indicating the existence of a negative relationship. This contradicts hypothesis seven (H7) of the thesis which postulates that the tenure of independent directors has a positive relationship with the diversification value. This result is in line with the study of Huang (2018); Hwang and Kim (2009) and Fracassi and Tate (2012). This could be as a result of increased familiarity between the board and management that can undermine board independence and can be associated with a decrease in firm value. Another possible

reason is that for firms with short-tenured boards, the marginal effect of board learning dominates entrenchment effects (Ozkan, 2011), whereas for firms that have long-tenured boards, the opposite is true. Moreover, it can be argued that the entrenchment effects of long board tenure could be higher in family firms compared to non-family firms in the Malaysian capital markets because family controlling shareholders have the incentives to exert more influence on the independent directors due to their interest in managing the firm in their own way to fulfil their private objectives at the expense of minority shareholders (Anderson et al., 2004).

The next important variable used by the study is the managers' wealth maximization. The result on the relationship between managers' wealth maximization and firm value display a statistically positive relationship at 5%, 1% and 10% for model 1, model 2 and model 3 respectively. This finding is consistent with prior studies (Li, 2007; Kuo, Li, & Yu, 2013; Gao & Li, 2015; Brick, Palmon & Wald, 2018). The result indicates that every stakeholder of a firm creates value for the company, as managers are considered to be stakeholders of a firm. According to the stakeholder's theory the managers are also affected by the outcomes of the firm. A positive firm performance will eventually make their position stronger. This will make the probability of him being fired smaller. Thomsen and Conyon (2012) describe that the view of corporate expenditure of CEO's change when they buy or receive company's stock. Thus changing the compensation structure or setting appropriate incentives for the CEO can give positive results to the firm.

This finding is also supported by Shaw and Zhang (2010), who find that manager compensation is positively related to firm performance. Carpenter and Sanders (2002), also

conclude that the pay-performance relation is significant and positive. These relationships are primarily explained by the alignment of managers and shareholders' interests by using efficient compensation contracts. The agency theory also supports this result, because it was stated that incentive schemes in the form of financial rewards to the directors would limit the difference in alignment.

When total corporate diversification is divided into two types of diversification; related and unrelated diversification, the result of the regression analysis shows that the related diversification has a positive and significant relationship with diversification value at 10% and 5% for model 1, model 2 and model 3 respectively. The result also supports hypothesis eight (H8a) of the study which assumed that the related diversification have a positive relationship with the diversification value. This finding is consistent with the results of prior studies (Collis & Montgomery, 1997; Palich et al., 2000; Miller, 2006; Dess et al., 2010; Almudena, 2016).

As predicted, that related diversification moves of Malaysian firms have been translated into profitability benefits. Since these companies have been immersed in an extremely fierce competitive environment during the period of study, their related diversification processes seem to have been the outcome of a rational profitability-seeking behaviour to survive and thrive in that business context so that profits derived from exploiting economies of scope have been greater than costs associated with its implementation (Mehmood, 2015). Moreover, related diversification could have had profitability advantages in Malaysia due to the reason been that developing countries are characterized by greater imperfections in the markets for capital, products and managerial talent, and

related diversified firms could have acted as intermediaries between individual entrepreneurs and imperfect markets Almudena (2016). Thus, our result supports the empirical findings of several previous studies from different countries that also find that related diversification predicts higher profitability.

Furthermore, the study found that the relationship between unrelated diversification and firm value is not statistically significant in model 1, model 2 and model 3 respectively. This has provided a justification for the rejection of hypothesis eight (H8b) of this study which presumed that the unrelated diversification has a positive relationship with the diversification value. Contrary to our arguments, unrelated diversification has not been as closely tied to growth benefits as was theoretically assumed. The previous studies by Geringer et al. (2000), Kim et al. (2004) and Almudena (2016) also find that the relationship between this strategy and firm growth is not statistically significant. This could be due to an inadequate implementation of internal mechanisms necessary to successfully manage unrelated diversification since, as with any other strategy, the extent to which its potential benefits are actually achieved depends largely on how effectively it has been implemented and managed (Almudena, 2016). One other possible explanation could be that, in general, the strategic objectives of such investments for Malaysian firms have been different during the period of study. So, the unrelated diversification moves of Malaysian firms could have been a defensive reaction to a perceived threat in a business reality characterized by mature, risky and inefficient markets rather than a means to achieve firm growth and to enable empire-building (Mehmood, 2015).

The last aspect that was conveyed by the regression analysis is the association of the control variables (CAGE, CSIZE & LEV) with firm value. Based on the outcome of the regression results, the corporate age does not show any significant relationship with the firm values in all the three dimensions. This indicates that corporation age does not determined any change in firm value of listed diversified PLCs in Malaysia.

The next variable that was controlled for in the study is the corporate size (CSIZE). Based on the regression result displayed, the CSIZE has negative coefficient with significance level of 1%, 5% and 5% for model 1, model 2 and model 3 respectively. This result congruent with the study of Mohd Ghazali (2010), Haniffa and Hudaib (2006) and Chang and Wong (2004). This indicates that larger firms are highly associated with better financial performance which may be due to the greater amount of capital owned by larger firms and their ability to diversify risks in more efficient way.

The study further control for leverage in the regression analysis of the study. The result shows that debt level (LEV) has a significant positive relationship with firm value in for model 1, model 2 and model 3 respectively. The positive result is consistent with the findings of John and Sebet (1998), Haniffa and Hudaib (2006) and Christensen et al. (2010), and Salina and Nazrul (2015). This finding is in line with the views of Jensen (1986) and Stulz (1990), that debt financing is an effective mechanism to improve firm value by controlling the manager's discretion over free cash flow and encouraging them to engage in more productive investment. Besides, managers with debt contracting show improved firm performance and become more efficient in avoiding bankruptcy. However, the possible explanation for this result is that the market tends to place higher valuations

on firms that operate at higher level of debts. This may also indicate that higher debt financing promises an increase in future firm growth and firm value, suggesting that the market places higher valuations on companies that use more leverage. In addition, the result also signals that Malaysian listed diversified companies that operate at high level of debt are able to acquire more advanced technology, and hence improve corporate value.

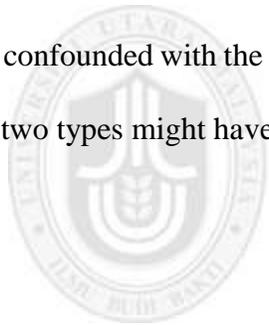
4.5.3 Relationship between Total Diversification and Diversification Value

The regression result also captured the results of the other category of the independent variables, which is the corporate diversification strategy. At first, the effect of total diversification (extent of product diversification strategy) on diversification value. Table 4.7 shows the results of three different simple linear regression models run to examine effect of total diversification on the three dimensions (sales, assets, EBIT) of firm value. It can be seen from the result that the effect of total diversification on any of the three dimensions was not significant. This has provided a basis for rejecting hypothesis eight (H8) of this current study which established that the total diversification had a positive relationship with diversification value. The significance for any of the regression model is not less than 0.05 (for 95% confidence interval) and is also not less than 0.10 (for 90% confidence level). These results are consistent with Marinelli (2011), Montgomery (1985), Chang and Thomas (1989), Lloyd and Jahera Jr. (1994), Çolak (2010), Mehmood (2015) and Patricia and Dastgir (2016) who also revealed insignificant diversification effects on firm value. Research by Marinelli (2011) and Mehmood (2015) that were more recent in this regard and it also relied on market as well as accounting measure of performance, and revealed that diversification was not a cause of performance, rather diversification – performance relationship was attributable to certain other factors.

Accordingly, Çolak (2010) suggested that effect of varying levels of diversification on performance was not a significant systematic phenomenon and there could be certain other crucial reasons along with diversification, such as poor performance, deficiency of innovation, and external economic conditions, which could explain company performance. Similarly, some other authors also supported the idea that diversification alone could not significantly depict performance unless it was coupled with certain other factors of supreme importance like managers wealth maximization (Choe et al., 2014; Li, 2007), corporate parenting (Mehmood, 2015; Nippa et al., 2011), managerial styles, management systems, organizational structures (Christensen & Montgomery, 1981), and internal organizational arrangements (Hill et al., 1992).

One of the other reasons for insignificant effect of diversification on performance could also be attributed to the fact that in examining product diversification overall, the total entropy score of total diversification was used. Whereas, this total diversification score is a combination of related diversification score and unrelated diversification score which are the scores for related diversification strategy and unrelated diversification strategy respectively. So, a significant effect of total diversification on firm value dimensions could not be found as total diversification was sum of related and unrelated diversification scores (Mehmood, 2015; Patrisia & Dastgir, 2016). This is in agreement with Park (2010) because the effect of total diversification strategy on firm value could not be correctly observed unless performance is examined against related diversification and unrelated diversification strategies separately.

The possible explanation about this finding is that when the study combines a positive relationship between related diversification and firm value with a negative relationship between unrelated diversification and firm value it will balance or diminish the effect. Patrisia and Dastgir (2016) further argue that the different direction of these two relationships may become the reason for an insignificant relationship between the level of total diversification and firm value. Hence, on the basis of these arguments and findings from previous studies, the insignificant effect of total diversification strategy on various dimensions of firm value could be justified. However, the possible implication of this finding is that the managers in general and Malaysian managers in particular must be cautious about the effects of diversification strategy. Effect of diversification strategy must not be confounded with the relative effect of related and unrelated diversification strategies as the two types might have different effects on firm value.



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Table 4.7
Regression Result on the Relationship between Total Diversification and Diversification Value

Variables	EVS Coefficient (t-value)	EVA Coefficient (t-value)	EVE Coefficient (t-value)
TD	0.01 (0.01)	0.02 (1.08)	0.01 (0.35)
Board Size	-0.07** (-3.67)	-0.11** (-4.31)	-0.05* (-2.41)
BI	0.55*** (5.35)	0.16** (3.94)	0.25* (1.87)
AIND	0.03*** (-2.55)	0.02* (-1.76)	0.02** (-2.24)
ASIZE	0.03* (-2.09)	0.06*** (-3.54)	0.02** (-2.21)
CEXP	0.03 (0.07)	0.02 (0.06)	0.05 (0.07)
RMC	0.05* (2.41)	0.28* (1.89)	0.36** (3.69)
TIND	0.08* (-2.13)	0.07*** (-3.90)	0.03** (-2.71)
MWM	0.15** (3.29)	0.23*** (6.19)	0.07* (2.45)
CAGE	0.02 (0.38)	0.03 (-0.75)	0.04 (-0.76)
CSIZE	0.04*** (9.07)	0.02*** (9.37)	0.24** (6.09)
LEV	0.38* (2.06)	0.02* (2.40)	0.06* (2.34)
Adj. R-squared	0.26	0.27	0.31
F-Stat.	0.00***	0.00***	0.00***
Observation	490	490	490

Where; TD= Total Diversification; Where BS= Board size; BI=Board independent; AIND=Audit committee independent; ASIZE= Audit Size; CEXP= CEO expertise; RMC=Risk management committee; TIND=Tenure of independent directors; MWM= Managers' Wealth Maximization; CAGE= Corporate age; CSIZE= Corporate size; EVS= Excess Value Sales; EVA= Excess Value Asset; EVE= Excess Value Ebit *,**,*** Indicates that the parameter estimates are statistically significance at the 1%, 5%, and 10% levels respectively.

Table 4.8
Comparison between expected and actual results

Variables	Acronyms	Expected Result	Actual Result
Board Size	BFSIZE	+	-
Board Independence	BIND	+	+
Audit Committee Independence	AIND	+	-
Audit committee size	ASIZE	+	-
CEO expertise	CEXP	+	Not significant
Tenure of independent directors	TIND	+	-
Risk management committee	RMC	+	+
Total diversification	TD	+	Not significant
Related diversification	RD	+	+
Unrelated diversification	UD	+	-
Manager's wealth maximization	MWM	+	+
Corporate size	CSIZE	+	+
Leverage	LEV	+	+
Corporate age	CAGE	+	Not significant

4.6 Testing Moderator Hypotheses

The test of moderator was done using Moderated Regression Analysis (MRA). Moderated Regression Analysis was conducted using interaction terms for moderator and independent variables, as proposed by Hair et al. (2010) and Sharma, Durand and Gur-Arie (1981). Interaction terms are usually developed by multiplying the independent variable with the moderating variable.

Three models were constructed. In the first model, the study entered first dependent variable which is one of the dimension variable (EVSASLES) for measuring firm value and all the predicting variables (Related diversification & unrelated diversification) as well as the moderating variable (managers' wealth maximization) along with the control variables (Age, Size & Leverage). This enabled examining effects of diversification

strategies over EVSales dimension, which was also one of the objectives of the study. In the second model, the study change the dependent variable which was used to proxy firm value to be the EVAsset with the other variables remaining unchanged as it was in the first model. Finally, in the third model, the study only changes the dependent variable with the third dimension variable (EVEBIT) while the remaining variables remain intact. Moderator effect was studied through increase in the third model's significance compared to first two models, significant change in F-statistics (for R^2 change), and/or through the significance level of interaction term. If the significance levels were achieved, the moderator effect was proved (Hair et al., 2009).

Apart from that, a moderator could be a pure moderator or a quasi-moderator. A 'pure moderator' changes the form of relationship between the dependent and independent variables. A pure moderator interacts with predictors and has negligible correlation with the dependent variable. (Sharma et al., 1981; Zahra, 1996). A 'quasi moderator' also modifies the form of the relationship between the dependent and Independent variables as it significantly interacts with independent variables, but it also possesses a significant relation with dependent variable (Sharma et al., 1981; Zahra, 1996). This study examines whether the moderator was a pure or a quasi-moderator. This was done by looking at the relationship between the moderator variables and dependent variables (Sarina, 2010; Sharma et al., 1981). The framework for identifying the moderator as pure or quasi moderator is presented in Figure 4.4.

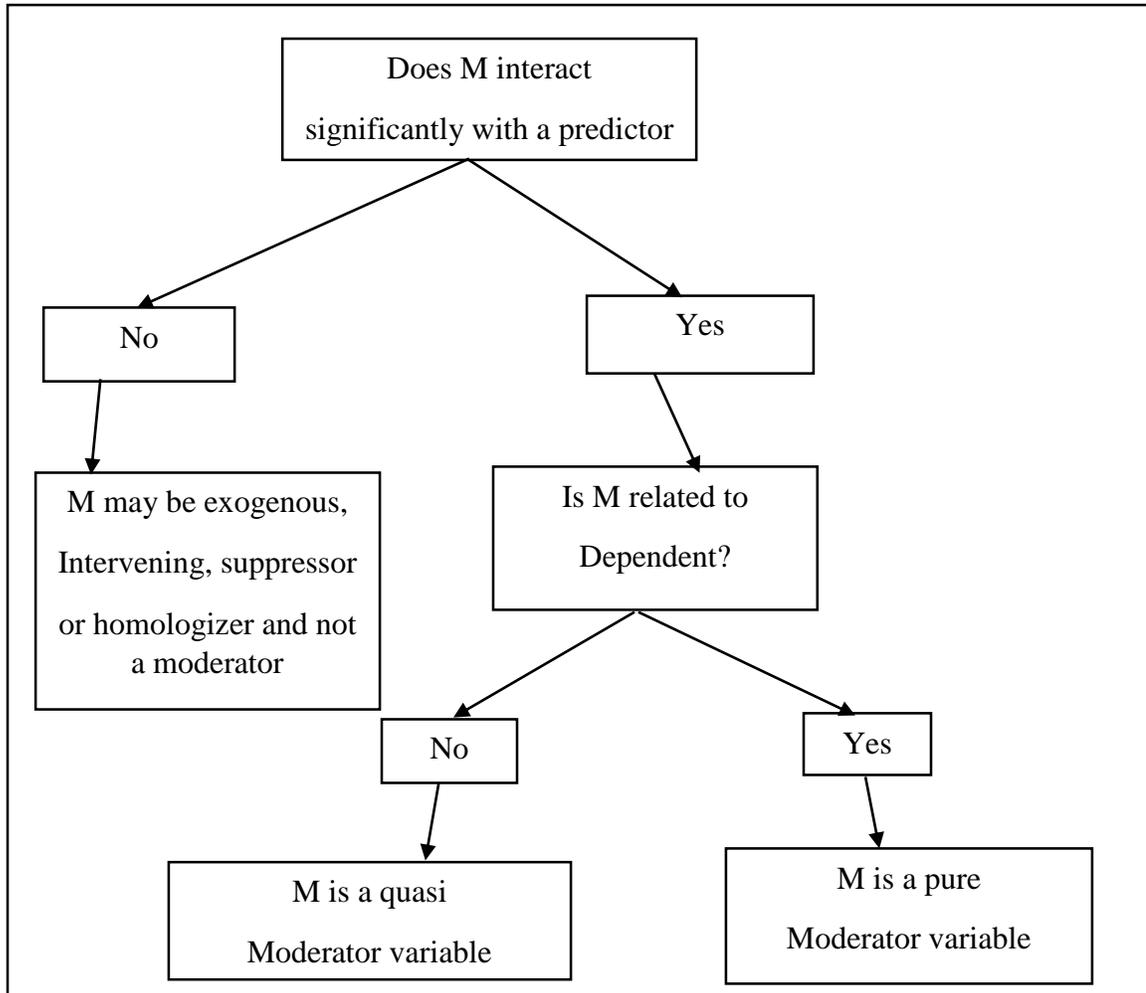


Figure 4.4
 Framework for Identifying Pure & Quasi Moderators
 Adapted from Sharma et al. (1981), pp. 297 and Mehmood (2015), pp.166
 Note; M= Moderator

Table 4.7 contains the results of the regression estimating the moderating impact between managers' wealth maximization and total diversification, related and unrelated diversification strategies and firm value. The result shows a significant moderating effect of manager's wealth maximization on the related diversification and firm value link at 5%,

5% and 1% in model 1, model 2 and model 3 respectively. This supports hypothesis nine (H9a) which presumed that managers' wealth maximization positively moderates the relationship between related diversification and diversification value. Specifically, the positive and significant coefficient for the interaction term would suggest that the greater the value of the manager's wealth maximization the greater the positive effect of related diversification on firm value. Normally, positive relationship between the variables can be explained by the efficiency of the corporate governance, which means that when the other governance arrangements are in force and effective, there is not much leeway for the managers to take an action to achieve their own benefits at the cost of the shareholders (Mehmood, 2015).

However, as it may be understood, there are no such forces because of the under-developed governance mechanism in the developing nation's case. Related to this point, a high-centralized ownership structure is supposed to enforce a kind of constraints on the managers' behavior. However, after controlling for this, government shareholding effect, the positive relationship still holds true. Thus, the study shows that in Malaysian's market, due to some institutional arrangements that have not been covered in the literature, such as the unique Malaysian culture, organizational characteristics, business philosophy or other social-economic factors, Malaysian managers may not necessarily behave in the same way as those in the other markets.

Another possible explanation is that corporate managers understand the critical success factors of businesses well, and the businesses also provide the opportunities for value addition (Campbell, 2007; Johnson et al., 2008). They need to continuously possess that

knowledge, skills, resources and competences with which they could add value to related businesses (Alexander et al., 1994; Campbell, 2007). Naturally, this seems to be more possible when the portfolio of businesses is operating in related markets or sectors and the businesses also share common internal characteristics. Therefore, a role like managers' wealth maximization was suggested to be a moderator for related diversification strategy by past scholars (Li, 2007; Ueng & wells, 2001) and the findings of this study have proved the proposition.

On the other hand, the interaction term between unrelated diversification and diversification value indicate a negative coefficient with a statistical significance of 10% for model 1, model 2 and model 3 respectively. This has provided a basis for rejecting hypothesis nine (H9b) of this study which established that managers' wealth maximization positively moderates the relationship between unrelated diversification and diversification value. Meanwhile, the negative coefficient would suggest that the lower the value of the managers wealth maximization variable (that is, the closer the diversifying manager is to the agent model), the greater the positive effect of unrelated diversification on firm growth. Although the main effects of unrelated diversification and manager's wealth maximization are not significant, the combined effect of both variables negatively affects corporate growth.

An unrelated or conglomerate diversification takes an organization away from its existing strategic capability and results into new businesses and entirely different market segments (Pearce II & Robinson Jr., 2011; Thompson et al., 2012). In unrelated diversification, the portfolio of businesses might keep on changing as the purpose of this strategy is not

attainment of functional or operative synergies but financial synergies and financial economies through restructuring (Bamford & West, 2010; Berger & Ofek, 1995). The managers might keep on searching actively for undervalued assets or businesses and continuously involve in buying and selling for gaining financial economies or benefits.

Meanwhile, unrelated diversification strategy could be successful with manager's wealth maximization role, as in this strategy there is no serious intention from the top management to create operational synergies rather the management is interested to seek undervalued businesses and assets for getting financial rewards through their trade (Bamford & West, 2010). Hence, this role is suitable for unrelated diversification strategy as it aims to attain financial synergies by combining cash flows of different businesses in the corporation (Gottschalg & Meier, 2005; Hoskisson et al., 2009). Hence, this would possibly leads to an adverse effect on diversification. However, it is better to create internal efficiencies among unrelated businesses by maneuvering cash across them, instead of striving to get economies of scope among those unrelated businesses (Ng, 2007; Tallman & Li, 1996).

Table 4.9***Results of Second-Stage Regressions Showing the Moderating Effect of MWM***

Variables	EVS	EVA	EVE	EVS	EVA	EVE
	Coef. (t-value)	Coef. (t-value)	Coef. (t-value)	Coef. (t-value)	Coef. (t-value)	Coef. (t-value)
RD	0.04 (2.06)*	0.03 (2.05)*	0.38 (3.71)**	0.04 (2.06)*	0.03 (2.05)*	0.38 (3.71)**
UD	-0.04 (-1.00)	-0.01 (-0.41)	-0.03 (-0.33)	-0.04 (-1.00)	-0.01 (-0.41)	-0.03 (-0.33)
Board Size	-0.07** (-3.67)	-0.11** (-4.31)	-0.05* (-2.41)	-0.07** (-3.67)	-0.11** (-4.31)	-0.05* (-2.41)
BI	0.55*** (5.35)	0.16** (3.94)	0.25* (1.87)	0.55*** (5.35)	0.16** (3.94)	0.25* (1.87)
AIND	0.03*** (-2.55)	0.02* (-1.76)	0.02** (-2.24)	0.03*** (-2.55)	0.02* (-1.76)	0.02** (-2.24)
ASIZE	0.03* (-2.09)	0.06*** (-3.54)	0.02** (-2.21)	0.03* (-2.09)	0.06*** (-3.54)	0.02** (-2.21)
CEXP	0.03 (0.07)	0.02 (0.06)	0.05 (0.07)	0.03 (0.07)	0.02 (0.06)	0.05 (0.07)
RMC	0.05* (2.41)	0.28* (1.89)	0.36** (3.69)	0.05* (2.41)	0.28* (1.89)	0.36** (3.69)
TIND	0.08* (-2.13)	0.07*** (-3.90)	0.03** (-2.71)	0.08* (-2.13)	0.07*** (-3.90)	0.03** (-2.71)
MWM	0.31 (5.39)***	0.21 (3.76)**	0.21 (5.28)***	0.31 (5.39)***	0.21 (3.76)**	0.21 (5.28)***
RD*MWM				0.02 (3.90)**	0.02 (3.19)**	0.05 (4.25)***
UD*MWM				-0.08 (-2.66)*	-0.03 (-2.23)*	-0.02 (-2.44)*
CAGE	0.02 (0.24)	0.23 (0.67)	0.02 (0.18)	0.02 (0.24)	0.23 (0.67)	0.02 (0.18)
CSIZE	0.02 (3.91)**	0.03 (2.34)*	0.02 (9.93)***	0.02 (3.91)**	0.03 (2.34)*	0.02 (9.93)***
LEV	0.01 (2.40)*	0.03 (2.56)*	0.01 (2.67)*	0.01 (2.40)*	0.03 (2.56)*	0.01 (2.67)*
Constant	(6.07)***	(5.36)***	(5.30)***	(6.07)***	(5.36)***	(5.30)***
Observations	490	490	490	490	490	490
Adjusted. R ²	0.37	0.42	0.41	0.37	0.42	0.41

Where; TD= Total Diversification; RD= Related diversification; UD= Unrelated diversification; BS= Board size; BI=Board independent; AIND=Audit committee independent; ASIZE= Audit Size; CEXP= CEO expertise; RMC=Risk management committee; TIND=Tenure of independent directors; MWM= Managers' Wealth Maximization; CAGE=

Corporate age; CSIZE= Corporate size; EVS= Excess Value Sales; EVA= Excess Value Asset; EVE= Excess Value Ebit.

4.7 Comparison of Related against Unrelated Diversifiers on Diversification Value

For this analysis, initially the companies were divided into two groups i.e. dominant related diversifiers and dominant unrelated diversifiers on the basis an entropy scores. However, for ease of interpretations, dominant related diversifiers are only termed as related diversifiers and dominant unrelated diversifiers are termed as unrelated diversifiers. Group statistical analysis was conducted for comparing their mean performance of these groups on each of the three dimensions of firm value. Table 4.11 shows that the group mean for RD (Related Diversifiers) is greater than the group mean for UD (Unrelated Diversifiers) on the following firm value dimensions as, EVasset and EVEbit, but surprisingly, the means for both the groups are exactly same on EVsales. Based on the result as revealed in table 4.11, it can be concluded that related diversification strategy is more superior over the unrelated diversification strategy. These findings are in line with the views from prior studies conducted by (Berger & Ofek, 1995; Mehmood, 2015; Almudena, 2016).

Table 4.10
Group Statistics of Related Diversifiers and Unrelated Diversifiers for Corporate Performance Dimensions

Variable	Group	Observation	Mean	Standard. Deviation
EVSales	RD	327	3.59	0.61
	UD	317	3.59	0.61
EVAsset	RD	409	2.49	0.69
	UD	317	2.45	0.7
EVEbit	RD	327	2.3	0.96
	UD	317	2.29	1.03

Where: EVSales= Excess value using sales multiplier; EVAsset= Excess value using asset multiplier
EVEbit= Excess value using earnings before interest and tax multiplier

To further to compare the superiority of the two diversification strategies, we consider the effects of their coefficient and the effect of the t-value on diversification value. Based on the result from table 4.6, related diversifiers have a positive significance level at 10%, 10% and 5% for model 1, model 2 and model 3 respectively. While the unrelated diversifiers do not maintain any significant impact on firm value. In addition, the result is also in favor of the superiority of related diversifiers over the unrelated diversifiers. The t-value result indicates that for any significant relationship, the related diversifiers have an impact of 16%, 12% and 15% on diversification value respectively. Based on this result, therefore it could be established that related diversifier performed better than the unrelated diversifiers, this supports the findings of Rumelt (1982), Galván et al. (2007), Mishra and Akbar (2007), Mehmood (2015) and Almudena (2016).



4.8 Summary of Hypotheses Tests' Results

In order to get a collective understanding of results produced by this research, a summary of results for all the hypotheses tested in this research is presented in Table 4.11.

Table 4.11

Summary of Hypotheses Tests Results

No. Hypo. Nos.	Statement of hypotheses	Results
Hypotheses concerning effect of Corporate Governance on Firm Value		
1. H₁	Board size have positive impact on diversification value	Not supported
2. H₂	Board independence have positive impact on diversification value	Supported
3. H₃	Audit independent have positive impact on diversification value	Not supported
4. H₄	Audit committee size have positive impact on diversification value	Not supported
5. H₅	CEO Expertise have positive impact on diversification value	Supported
6. H₂	Risk management committee have positive impact on diversification value	Supported
7. H₇	Tenure of independent directors have positive impact on diversification	Not supported
8. H₈	Total Diversification have positive impact value	Not supported
8a. H_{8a}	Related Diversification have positive impact on diversification value	Supported
8b. H_{8b}	Unrelated Diversification have positive impact on diversification value	Not supported
9a. H_{9a}	Managers wealth maximization have positive moderating impact between related diversification and diversification value	Supported
9b. H_{9b}	Managers wealth maximization have positive moderating impact between unrelated diversification and diversification value	Not supported

4.9 Chapter Summary

The chapter started by discussing explanations on the descriptive statistics. This was followed by discussions on basic assumptions for multiple regression analysis, moderating, explanatory and control variables. It then proceeded towards presenting the results and discussions on multiple regression results. After that, findings and results were presented in a comprehensive manner for various hypotheses tests including that of moderator hypotheses and t-tests for comparing performance of different groups of companies. Finally, it presented a summary table for all the actual outcome of the hypotheses tested in order to get an overall view of the findings.



CHAPTER FIVE

SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1 Introduction

This final chapter presents the overview, summary, conclusion and recommendations of the study. The chapter also detailed the contributions, implications and limitations of the investigations, as well as suggestions for future research.

5.2 Overview of the Study

This study examines the relationship between corporate governance, corporate diversification and the value of diversified Public Listed Companies (PLCs) listed on Bursa Malaysia's Main Market. The study extends previous researches by simultaneously considering the monitoring mechanisms, namely, board and audit independence, board and audit size, tenure of independent directors, risk management committee, CEO expertise, in addition to corporate diversification strategies which comprises both related and unrelated diversification strategies and firm value which also has three dimensions (excess value sales, excess value assets & excess value earnings before interest and tax). Furthermore, based on the assumption that manager's wealth maximization plays a vital role in the level and choice of diversification strategies, which in turn have a long term effects in firm performance and the interest of shareholders, this study uses regression analysis to examine the moderating effect of manager's wealth maximization role on the relationship between corporate diversification strategies and firm value.

Consistent with agency theory and with prior evidence regarding the effect of certain characteristics of board of directors and audit committee and CEO characteristics, the present study suggests that the core mechanisms of corporate governance are specially designed to overcome the severity of agency problems in modern corporations. Meanwhile, the agency problems ascend due to the separation of ownership and control which results in a potential clash of interest between owners and managers. Managers who quest for self-interests are doubtful to maximize returns to shareholders as they have a tendency to misuse corporate assets, through involvement in high risk or imprudent investment to the detriment of capital providers. Though the conflict of interest may decrease firm's value and interfere with corporate investment strategy. In accordance, a good corporate structures and procedures are indispensable in order to protect the shareholders' interest and reduce the possibility of loss in firm value due to the separation of ownership and control.

5.3 Discussions on the Findings

As stated before, this section is mainly devoted to discussions on the results of hypotheses tests and on certain other important statistics. It has been mentioned earlier that the analyses was conducted using certain descriptive statistics, correlation analysis, scatter plots and graphs, simple linear regression and mainly relying on moderated regression analysis (MRA) which is based on regression analysis so as to test the moderating effect of managers' wealth maximization roles on the relationship between diversification strategies and dimensions of diversification value. The discussion is made on each hypothesis by relating it to the findings of the previous studies in the field, to underpinning theories of the concerned variables, and through adding justifications and reasons for each of the findings.

5.3.1 Discussions on the Effect of Governance Mechanisms on Diversification Value

The first finding relates to the relationship between corporate governance mechanisms and corporate diversification value. The items considered under corporate governance mechanisms are board characteristics, audit committee characteristics and CEO characteristics. The diversification value is measured with three multipliers of excess value (sales, assets & EBIT). On the part of the influence of board characteristics on diversification value, the study partially supports the influence of board characteristics on diversification value. The variables measured under board characteristics are board size, board independence, risk management committee and the tenure of independent directors. The empirical evidence suggests that board independence has positive and significant association with diversification value. This signals that independent directors on corporate boards minimize agency problems and protect the interest of all stakeholders.

On the part of board size, the result does not support the position that large boards are positively associated with firm value. The results suggests that larger boards exist even though they are value reducing, because they are necessary for some type of companies and under certain conditions. The negative association of board size with diversification value, may be due to some other exogenous factors. As board size increases above an ideal value, many problems may surface in relation to effectiveness & efficiency which could outweigh the benefits of having more directors on the board.

The next variable is the risk management committee, the result suggests that setting risk management committee have a positive effect on diversification value. Consistent with a risk-based approach, a board that puts in place firm-wide risk management system

increases risk awareness within a firm. This increase in awareness and knowledge allows the board for more sound decision making and creates a positive impact on the governance structures and on control environment of the firm. This, in turn, reduces the likelihood that uncontrolled business risks cause unexpected losses, reputational damage or strategic setbacks. On the part of tenure of independent directors, the result does not support the position of a positive relationship with diversification value. This could be as a result of increased familiarity between the board and management which may undermine board independence.

The second aspect of corporate governance mechanisms for this study is the audit committee characteristics. The result of the study partially supports the influence of audit committee characteristics on diversification value. The variables considered under audit committee characteristics are audit committee independence and audit committee size. The empirical result from this study documents a contrary position. The possible explanations for this finding may be as a result of the issue of expertise (the combination of education and experience) of the independent directors. The next variable under the audit committee characteristics is audit committee size. The regression result shows that audit committee size maintains a negative and significant relationship with diversification value. This indicates that the size of audit committee members is negatively impacting on the value of listed diversified firms in Malaysia. The implication of this result is that, larger audit committees are better at reducing firm value.

The third element of corporate governance mechanisms used in this study is the CEO characteristics. The CEO financial expertise is used to proxy the CEO characteristics. The

regression result does not provide statistical support that CEO financial expertise improves firm performance. The possible reason may be as a result of concentrated ownership structure of firms in Malaysia. Therefore, many CEOs may prefer to serve their own interest or the interest of the family when the disclosure is capable of exposing their dealings (Maigoshi, 2017).

5.3.2 Discussions on the Effect of Total Diversification on Diversification Value

The regression also captured the results of the other category of the independent variables, the effect of total diversification on firm value. The regression result does not provide evidence that total diversification has positive association with diversification value. The possible explanation for the insignificant effect of diversification on firm value could be attributed to the fact that in examining product diversification overall, the total entropy score of total diversification was used. Whereas, this score is a combination of related diversification score and unrelated diversification score which are the scores for related diversification strategy and unrelated diversification strategy respectively. Therefore, a significant effect of total diversification on firm value could not be found as total diversification is the sum of related diversification and unrelated diversification scores, because the effect of total diversification strategy on firm value could not be correctly observed unless performance is examined against related diversification and unrelated diversification strategies separately.

5.3.3 Discussions on the Effect of Diversification Strategies on Diversification Value

When total diversification is divided into two types of diversification; related and unrelated diversification. The result of the regression analysis shows that the related diversification

has a positive and significant relationship with diversification value. As predicted, that related diversification moves of Malaysian firms have been translated into profitability benefits. Since these companies have been immersed in an extremely fierce competitive environment during the period of study, their related diversification processes seem to have been the outcome of a rational profitability-seeking behaviour to survive and thrive in that business context. The study further found that the relationship between unrelated diversification and firm value is not statistically significant. Contrary to our arguments, unrelated diversification has not been as closely tied to growth benefits as was theoretically assumed. This could be due to an inadequate implementation of internal mechanisms necessary to successfully manage unrelated diversification since, as with any other strategy, the extent to which its potential benefits are actually achieved depends largely on how effectively it has been implemented and managed.

5.3.4 Moderating Effect on Diversification Strategies and Diversification Value

This study finds that the moderating variable have different statistical effects on the independent variables (related and unrelated diversification) against the dependent variable (diversification value). The result shows a significant moderating effect of managers' wealth maximization on the related diversification and diversification value relationship. Specifically, the positive and significant coefficient for the interaction term would suggest that the greater the value of the managers' wealth maximization the greater the positive effect of related diversification on diversification value. Normally, positive relationship between the variables can be explained by the efficiency of the corporate governance. This means that when the other governance arrangements are in force and effective, there is not

much leeway for the managers to take an action to achieve their own benefits at the detriment of the shareholders.

On the other hand, the interaction term between unrelated diversification and diversification value indicate a negative coefficient with a statistical significance. Meanwhile, the negative coefficient would suggest that the lower the value of the managers wealth maximization variable (that is, the closer the diversifying manager is to the agent model), the greater the positive effect of unrelated diversification on firm growth. Although the main effects of unrelated diversification and manager's wealth maximization are not significant, the combined effect of both variables negatively affects corporate growth. Meanwhile, unrelated diversification strategy could be successful with manager's wealth maximization role, as in this strategy there is no serious intention from the top management to create operational synergies rather the management is interested to seek undervalued businesses and assets for getting financial rewards through their trade. Accordingly, to increase the diversification value of the company, a manager should give more attention to related diversification which has a positive and significant impact on corporate diversification value. Even though unrelated diversification strategy has a negative impact on diversification value, it also has a significant relationship. Hence a manager may also be concerned with unrelated diversification in order to maintain corporate diversification value.

5.4 Contributions

This study extends the contributions of previous studies in several ways. The discussion of the contributions is divided into methodological contributions, theoretical contributions and practical and policy implications.

5.4.1 Methodological Contributions

The first contribution of this study is that it focuses on a single East Asian country, unlike previous studies that have linked corporate governance and corporate diversification (Claessens et al., 1999; Lins & Servaes, 2002), which pooled data from several countries. Although, studies on corporate studies on corporate diversification by Ishak and Napier (2006) separately analyze Malaysian companies with corporate diversification and corporate governance. Mehmood and Hilman (2015) analyze corporate diversification strategies and corporate parenting. Doaei, Davarpanah and Sabzi (2017) examines the approach of corporate diversification and its efficiency in bursa Malaysia. Meanwhile, these prior studies did not link corporate diversification strategies with corporate governance and diversification value. The findings of the present study on corporate governance issues and corporate diversification for Malaysian companies are therefore not distorted by data from other countries.

Moreover, to the best of the researcher's knowledge, this study is the first of its kind that documents the moderating effect of manager's wealth maximization on the relationship between corporate diversification strategies and diversification value. Previous studies such as Becerra and Santalo (2004), Li and Rwegasira (2008), David et al. (2010), and Mehmood (2015) incorporated certain moderators such as corporate parenting, market

structures and control system into the relationship between corporate diversification and firm value. The present study has contributed to the existing literature on moderating role of manager's wealth maximization on the relationship between corporate diversification and diversification value.

In addition, to the best of the researcher's knowledge, there was no any previous study that documented the extent of corporate diversification strategies and its effects on diversification value, measured with excess value (sales, assets & earnings multipliers). This study is the first of its kind that fills in this literature gap by documenting the level of corporate diversification strategies and its effects on firm value. More over this study provides evidence on related diversification strategy positively influences corporate diversification value (as measured by excess value), whereas unrelated diversification strategy negatively influences diversification value. Further, it shows that relatedly diversified companies were significantly different and seem to outperform unrelatedly diversified companies on firm value measures.

Furthermore, previous studies have concentrated on the use of financial indicators to measure firm value (Berger & Ofek, 1995). Recently, few efforts have been put in place to measure corporate diversification value with excess value (see for example Berger & Ofek, 1995; Ishak, 2004; Ishak & Napier, 2006; Stowe & Xing, 2006). This study has contributed to the recent trend in corporate diversification strategies studies by using all the three industrial multipliers (sales, assets & earnings) to measure excess value. Examining diversified firm with excess value has several advantages over the accounting measures (Berger & Ofek, 1993). Using the industry multiplier approach on individual business

segments has several advantages over other methods. For instance, studies that assess value effects using accounting and market based methods provide only limited opportunities to examine the potential sources of gains or losses from diversification. The industry multiplier approach not only provides a direct estimate of the excess value associated with diversification, but also allows further investigation at the segment level of the sources of any overall value effect (Stowe & Xing, 2006).

With the exception of Anderson et al. (2000), Ahmad et al. (2003), previous studies do not examine board variables as mechanisms in governing corporate diversification. However, there are studies that examine the effect of board mechanisms on other strategic decisions, such as the acquisition of other companies (Zantout & O'Reilly-Allen, 1996; Ishak & Manaf, 2013), tender offer bids (Byrd & Hickman, 1992; Finkelstein, Hambrick, & Cannella, 2009), and corporate R & D strategy (Hoskisson et al., 1991). In most previous studies the impact of board monitoring was measured using board size, proportion of outside directors and duality of leadership. This study includes further board mechanisms relevant to corporate governance, with more detailed attributes as used in Ishak (2004). These are board characteristics (tenure, independence, size and risk management committee), audit characteristics (independence, and size) and CEO characteristics (expertise).

5.4.2 Theoretical Contribution

The theoretical contributions discussed in this section are drawn from the review of the literature and the findings of the analyses. This study has contributed to the agency theory in corporate governance literature. Although plenty of literature addresses the issues of

corporate governance using agency theory, most of the studies are focuses on developed countries, which have different environment from non-developed countries. This present study has added to the understanding of agency theory in a developing country, where companies are controlled by controlling owners, so that agency relationships become complex (Ishak, 2004). There is an alliance between management and the controlling owner, with minority shareholders on the outside facing the danger of expropriation.

The study contributes to the agency theory by identifying the factors that can be used to mitigate agency costs. In an organizational settings that presents an opportunity for insiders to expropriate the wealth of the firm at the expense of outsiders, the findings of the study show that board independence can be used to minimize the agency costs. On the other hand proved that CEO characteristics cannot be relied upon to mitigate the agency problem in the countries with concentrated ownership. Furthermore, the study extends the understanding of the techniques to expropriate the firm. Hence, having good governance, effective corporate governance contributes to sustainable economic development by enhancing the stability and performance of companies, reduces the risk of financial crises, and further leads to better relationships with all stakeholders.

Moreover, this study contributes to the resource dependency theory. Though, the study does not document the influence of board size on firm, it provides empirical evidence that the size of audit committee members is negatively impacting on the value of listed diversified firms in Malaysia. This could be due to some audit committee members may be bedeviled with the problem of not having the necessary skills, knowledge and experience to act as audit committee members and perform their duties optimally. Similarly, the

existence of management challenge to an apparent lack of available non-executive directors (NEDs) with the required business acumen and accounting background who are willing to serve on audit committees. This stress the need for firms to source for directors with requisite experience and expertise for counselling and advising role that will eventually improve the firm value.

This study supports the assumption under transaction cost economic, that a diversified organization might be more efficient compared to a single segment firm and could make better investment decisions because it has its own internal capital market (Kuppuswamy & Villalonga, 2010) with the help of which, it could make successful allocation of resources across different businesses to improve its performance (Galván et al., 2007). Varanasi (2005) added that diversification could lead to creation of interaction economies through simultaneous supply of inputs and processes across different units. Diversified organization could also gain performance benefits by combining businesses which have different flow of earnings or lowering variation in year by year cash inflows (Mackey, Barney & Dotson, 2017). Diversification through backward and forward integration might lead to better performance through savings in production and transaction costs because in industries where the organization is working might be engaged in customer-supplier relationships (Fukui & Ushijima, 2006).

Based on the discussions of market power theory, this study supports some of the suggestions that there could be various motives, benefits and or consequences for pursuing diversification strategies. Related diversifiers might perform better as compared to single segment firms as per they achieve increased market power and resource management

benefits. In addition, diversified firms performed better in emerging economies as they enjoy the benefit of lower internal transaction costs and efficient internal markets (Mehmood, 2015). Diversified firms have conglomerate power which makes them thrive on their diversity (Purkayastha, Manolova & Edelman, 2012; Knecht, 2013). In his own view, Gribbin (1976) says a firm will not have conglomerate power if it does not hold significant positions in a number of markets. This power then propels the firm to enter new markets through predatory strategies supported by its position, resources and strength in its current market (Mulwa, Tarus & Kosgei, 2015).

Every stakeholder of a firm creates value for the company. Since management are considered to be stakeholders of a firm, the manager is also included in this consideration. Thus according to this theory the manager is also affected by the outcomes of the firm. A positive firm performance will eventually make his position stronger. This will make the probability of him being fired smaller. Besides, this can also be applied to the topic regarding managers' wealth maximization and firm performance. Thomsen and Conyon (2012) describe that the view of corporate expenditure of managers' change when they buy or receive company's stock. Thus changing the compensation structure or setting appropriate incentives for the managers can give positive results to the firm. Accordingly, the outcome of this study throws more weights to this postulation, thereby contributes to the exist discussions on this theory.

Further, this study contributes by integrating multiple theories, in order to aid in the provision of better understanding of the dynamism of corporate mechanisms, corporate diversification and diversification value. Hence, this justifies the use of both agency, resource dependency, stakeholders, transaction cost economic and market power theories

as a guide to this research work. Hence, the findings provided new insights into corporate mechanisms, corporate diversification and firm value relationships by confirming the moderating role of manager's wealth maximization roles into the relationship.

The results of this research also support the notion that diversification strategies – diversification value relationship is influenced by contingency factors or moderators (Martínez-Campillo & Fernández-Gago, 2008; Ravichandran et al., 2009; Mehmood, 2015). Specifically, this research agrees with and confirms the proposition that product diversification – diversification value relationship is moderated by managers' wealth maximization (Li, 2007). Moreover, the findings of this study suggest that Resource Based View (Wernerfelt, 1984), Transaction Cost Economics (Williamson, 1971), Market Power View (Martin & Eisenhardt, 2001) and stakeholders view (Friedman, 1970; Freeman, 1984; Puyvelde et al., 2012) can be used in explaining the relationship between diversification strategies, managers' wealth maximization roles and corporate diversification value. This extended the body of research on the topic as well as paid a significant contribution to the relevant theories. There was substantial body of research on the relationship, but the studies were limited regarding interrelationships between product diversification strategies, corporate level competences or managerial styles, corporate parenting and firm value (Menz & Mattig, 2008; Liu & Hsu, 2011; Mehmood & Hilman, 2015).

Most importantly, it possessed a gap in form of lack of research on the moderating role of manager's wealth maximization roles into product diversification – diversification value relationship. This study has filled that research gap by bringing together factors of extreme

strategic importance, which are product diversification strategies, manager's wealth maximization and diversification value together into one unique framework. At the same time, it has significantly contributed to the relevant theories in the field.

The findings of this study does not provide evidence that diversified companies are traded at a discount as happens in the USA and the UK, and demonstrate that in a developing country like Malaysia, diversification is perceived to be a blessing. Given the inter-relatedness of many companies, it may still be more efficient for substantial investors to achieve the benefits of a diversified portfolio through firm-level diversification rather than capital market diversification (Ishak & Napier, 2006). Hence, diversification may be regarded as positive and/or more appealing. On the other hand, diversification may be used by controlling shareholders as a strategy for extracting value from companies at the expense of minority shareholders. The evidence suggests that diversification is still, in Malaysia, perceived to be a contributor to firm value rather than value-reducing.

5.5 Practical and Policy Implications

The findings of this study have implications for researchers, regulatory agencies and practitioners.

The findings of this study highlight a number of practical issues with many practical implications. First, the study exposed some potential areas of improvements for Malaysian code of corporate governance. It is apparent that the code places more emphasis on the board independence and independence of audit committee than the level of members' financial expertise. However, the findings of the study highlight the importance of financial

expertise more particularly in the areas with financial technicalities that requires deep financial knowledge to identify any breaches of fraudulent activities in those areas. In view of the forgoing, this study recommends that Security Commission of Malaysia should in the forthcoming code recommend for the redefine of financial expert as (i) person with a minimum of bachelor degree or professional qualification in accountancy or other finance related fields. (ii) a person with at least five (5) years' experience in the finance-related position or industry. The Commission should also recommend for an increase in the required number of persons with the professional qualification in the audit and board committee to at least two persons. This is to allow the professionals to have a thorough review of the firms' financial activities and enjoy the benefit of shared responsibility.

Secondly, the study points towards effects of product diversification strategy on firm value and caution managers that they might not be able to see the effect of total diversification strategy on corporate value unless they differentiate between and segregate total diversification strategy into related diversification strategy and unrelated diversification strategy. Managers must adopt restraint in selecting their diversification routes as related diversification adds positively to firm value. On the other hand, as also revealed by most of the past studies, unrelated diversification affects corporate performance negatively (Mehmood, 2015). Hence, corporate diversification, particularly in the Malaysian context, is recommended in related sectors and industries instead of unrelated ones.

Since diversification is being guided by resources and capabilities of an organization, it may choose to diversify into similar or different industries if it possesses excess resources and capabilities that it could utilize profitably. Accordingly, the empirical evidence on the

superiority of related diversification strategy over unrelated diversification strategy contributes in assisting business managers and Malaysian CEOs, directors and corporate planners to get rid of the dilemma on their choice of the best and most suitable diversification strategies. Particularly, the understanding gained in the study regarding the relationship between diversification strategies and wealth maximization motive in apprehending the effect and using most appropriate strategy for adding value to their business.

Furthermore, for managers, this study highlights the importance of managers' wealth maximization roles diversification value. It is because the most important revelation of this study is the active part of managers' wealth maximization roles as moderators on the relationship between diversification strategies and firm value. In other words, managers' wealth maximization roles act as important contingency variables when it comes to product diversification – firm value relationship. The roles work along with diversification strategies to cast a combined effect on diversification value. For the Malaysian's firms, diversification is a way to improve productivity and efficiency more than a tool for the managers to achieve their own interests or a device to compete with the rivals. Thus diversification would be beneficial instead of value destroying.

5.5.1 Contribution to Malaysian Economic and other Developing Countries

On the basis of this research results, managers in general and Malaysian managers in particular are recommended to develop corporate level resources, skills and knowledge to directly add value to their businesses in case they are following related diversification strategy. This arrangement has a greater probability of assuring increased corporate

performance. However, in case they are going to follow unrelated diversification strategy, they must prepare to play the role of Portfolio Managers as this role is suitable for unrelated diversification strategy (Mehmood, 2015). Portfolio manager role is characterized by decentralization along with having corporate managers who actively seek acquisition of undervalued assets and businesses for generating financial economies. The portfolio of businesses keeps on changing as corporate managers buy and sell the businesses based on their financial performance.

This study has provided recommendations for PLCs operating in wide variety of sectors including various manufacturing as well as service related industries. Similarly, this research has attempted to refine the approach to corporate strategy formulation by the Malaysian corporate sector along with redefining the criteria to take capital investment decisions involving corporate level diversification. Likewise, the findings of this research might also be equally applicable to PLCs and corporate sectors in other developing countries facing similar business and macro environments like those in Malaysia. It is because the business group structure, like the one prevalent in Malaysia, is also a popular corporate structure in number of other Asian countries (George, 2007; Mishra & Akbar, 2007). Furthermore, taking all the guidelines of this research, Malaysian corporate sector could improve its contribution to country's GDP and ultimately help in attaining Malaysia's GDP growth targets along with providing help in realizing other national level programs such as Economic Transformation Programme.

Lastly, this study presents certain cautions and recommendations for managers in general and Malaysian managers in particular about the choice of diversification strategies and

manager's wealth maximization role. The study recommends that managers should prefer following related diversification strategy coupled with the manager's wealth maximization role for increasing their companies' performance. Therefore, the study's recommendations are serving as a guideline for the overall Malaysian corporate sector and are also extended to PLCs in similar developing countries.

5.6 Limitations of the Study

Every research usually possesses certain limitations. The findings of this thesis can be fairly interpreted with a better understanding of these research limitations. The limitations of this study are reported as thus;

Some limitations in the methodological limit the generalizability of the findings. First, the sample is limited to PLCs. The findings may not be applicable to small companies as well as unlisted companies. Secondly, the use of cross-sectional study for a single year may add some noise in generalizing the findings. However, it is not expected to be significant since the data of the companies were collected from the same year and companies were facing the same economic, market and legal situations.

There is insufficient information to determine the sources of bias and validity because the data were collected from secondary sources (Ishak, 2004). However, the main data sources of this study, companies, annual reports and the Thompson Reuters data base, are expected to be reliable. In addition, data needed for research purposes are not exactly similar to the available secondary data. Therefore, additional computation have been done, which might have led to computation error. However, as has been stressed in the previous chapter, the

work was carried out with great and was carefully checked. Moreover, this study uses only a disclosed information or secondary data approach, which does not enable respondents to convey their feelings, as no contact was made with the company.

Furthermore, this study uses only one variable from CEO characteristics and four variables from board composition and two variables from audit committee. It is possible that other corporate governance mechanisms such as gender diversity, ethnic diversity, audit financial expertise, internal audit function, internal audit source, ownership structure among other that are not consider in this contribute to corporate governance on firm value. Moreover, the data gathered from the annual report and the market might not be reflecting the real face of the corporate performance. These practical problems would influence the empirical test outcome to some extent.

This research examined relationships between those variables which are of general nature and are common or relevant to every PLC (namely product diversification strategy, manager's wealth maximization and firm value). Unlike U.S companies where diversification is measured at company level, in emerging economies like Malaysia, the diversification is measured at both company and group level (George, 2007; Mishra & Akbar, 2007; Mehmood, 2015). Therefore, the findings of this study are more applicable to those companies which are working in countries characterized by presence of business company groups.

In addition, the findings are more applicable to companies working in Malaysia and other countries with similar business environments and corporate cultures as in Malaysia. Finally, because this study uses cross-sectional data for a year, the measurement of

diversification is based on diversification status rather than diversification process (Ishak & Napier, 2006). Although there are limitations in the study, the findings, given the constraints of time and data, have provided necessary evidence on the relationship of corporate governance and corporate diversification in a Malaysian sample. However, this study provide some implications for future research.

5.7 Recommendations for Future Research

The present study could be extended in various ways. Future research could extend to other sample companies that were excluded from this study, such as financial service companies and non-listed companies. In addition, panel data for certain time-periods could be used because the more disclosure of governance and diversification is available beyond year 2017. Meanwhile, with time-period data, the measurement of diversification could not be limited to diversification status. It could be extend to examine the diversification process such as diversification changes, and the effect of mergers and acquisitions. Changes in governance mechanisms could also be examined.

Since diversification is a strategic operation, there is a variety of elements that influence the process of decision-making. However, only one (manager's wealth maximization) of those, which have been discussed before or covered in the existing researches, was included and discussed in this research. Apparently, there are still more need to find out about the rationale of diversification. Future research can examine such factors (efficiency achieving, competition advantage pursuing and the corporate parenting roles) that influence the rationality of corporate diversification. Future research in the context of emerging economies like Malaysia can also consider the variable of business group affiliation into

their frameworks. Although data on industry characteristics is usually limited in context of Asian countries but future research could look into studying the variables by adding certain industry and sectorial information in it if made possible by some data source.

Future studies could also attempt measuring diversification strategies and performance using more robust methods and try using more than one approach to measure related and unrelated diversification strategies to reveal more attention-grabbing results. Available literature indicates that as a future avenue of research there is need to carry out similar research on growth strategies in other industries such as banking which falls within the financial sector as well as in other regions in order to establish whether this link of growth strategies and performance can be generalized.

Finally, since there are high proportion of diversified firms in Malaysia which represents frequent diversification from those companies. Therefore, it is important to conduct future study that will unleash the outcomes of pursuing both product diversification and geographic diversification as well as their combined or interaction impact when they are implemented together so as to put convincing set of guidelines for Malaysian managers for taking diversification decisions.

5.8 Concluding Remark

This section discusses the major contributions, limitations, and recommendations for future research. Besides, the study provides insight on how corporate governance mechanisms and diversification strategies influence the diversification value, as well as the moderating effects of managers' wealth maximization on the relationship between diversification

strategies and diversification value in the Malaysian context. The findings contribute to the underpinning theories and the study is supportive of the view that enhanced corporate governance practices contribute towards increasing diversification value. In addition, evidence relating to the important role corporate diversification strategies play in shaping the expectations relating to firms, may be useful in assisting managers to get rid of the dilemma on their choice of the best and most profitable diversification strategies as well as their managerial decision making. Generally, this study provides additional insights to policy makers and regulators towards improving corporate governance policies in the future.



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