Comments on
Renee B. Adams and Hamid Meheran,
“Corporate Performance, Board Structure and its Determinants in the Banking Industry”

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Summary

- Empirical study on relation between board composition and firms performance in banking industry
- Findings: banking firms with larger boards do not underperform their peers in terms of market to book ratio
Surprising!

“Across these studies, a number of regularities have emerged—notably, the fact that board composition does not seem to predict corporate performance, while board size has a negative relationship to performance.” (Hermalin and Weisbach, Economic Policy Review, 2003)
The endogeneity of board size

- Carefully investigate the determinants of board structure
- M&A activity: it may leads to more persistent increases in board size
- Organizational structure of bank holding company
Robustness

- Even taking these potential endogeneity into account, performance is not negatively related to board size!
Clear messages

- No “one fits all” corporate governance structure form!
- At least, constraints on board size in the banking industry may be counter-productive.
Demsetz and Lehn (1985)

- If diffuse ownership structure is not efficient, and we would observe no diffuse ownership structure in a “rational world”! (Demsetz and Lehn, JPE, 1985)

- For non-financial firms, the smaller is the board size, the better the performance is. We should observe that board size should converge to three or 5.
Comments: endogeneity and econometric methodologies


- Board size and performance: better performing banks can afford to retain target directors longer around M&A
In particular, when the performance is extremely poor, for instance, in cases of accounting loss, there would be strong pressure to make the board slim.

Simultaneous equations for corporate governance structure and performance, instrumental variables, two-stage least squares, three-stage squares
Other comments

- Random effect models v.s. fixed effect models