BOARD INTERLOCKS AND FIRM PERFORMANCE

Research that will appear later this year in the *Journal of Management* shows that future firm performance will be more likely to decrease for firms with relatively higher resources in an interlocking partnership. In contrast, firms with relatively fewer resources than their interlocked partners will benefit from the interlock and are likely to experience a firm performance increase.

Key Takeaways:

- Board members who serve on multiple boards exert both positive and negative effects on firm performance, and these effects depend on the firm's relative resources.
- Firms with fewer resources perform better when their board members also serve on boards of firms with more resources.
- In contrast, firms with greater resources perform worse when their board members also serve on boards with more resources constraints.

Using data collected from 145 Italian manufacturing companies consistently traded on the Italian stock during the years 2001-2006, researchers examined the role of board interlocks (i.e., when a person is on the board of directors of two or more corporations) on ROA. Specifically, they found that when firms have relatively high available resources (calculated as the difference between the focal firm's available resources and the mean of available resources of interlocked partners), interlocking directorates reduced future firm performance. However, the opposite effect was found for the firms with relatively low available resources, suggesting that board interlocks are positively related to performance for firms with relatively lower levels of available resources, but negatively related to performance for firms with relatively high levels of available resources.

The research team also found more complex relationships among the relationships. For instance, the larger the discrepancy between available resources for the interlocked firms, the stronger the positive effect is for firms with relatively lower levels of available resources. Additionally, ownership concentration accentuates the positive results among resource-constrained firms, but attenuates the negative effects associated with resource rich firms.

Their analysis statistically controlled for aspects of the environment (like industry performance), the firm (like size and prior firm performance), the CEO (like nonduality), and the Board (like size and outsider ratio). The authors suggest that future research is needed to learn about the behavioral perspectives of corporate governance, and how executives use appointments on other boards to benefit themselves in terms of compensation and market visibility.

Source: Zona, F., Gomez-Mejia, L.R., Withers, M.C., (2015). Board interlocks and firm performance: Toward a combined agency-resource dependence perspective. *Journal of Management*, In Press.