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When elites forget their duties: The double-edged sword of prestigious directors on boards

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Citation

When Elites Forget Their Duties: The Double-Edged Sword of Prestigious Directors on Boards

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ABSTRACT Previous research indicates that the performance effect of prestigious directors is ambiguous. Our study addresses this issue by integrating the theoretical lens of board capital and the institutional perspective. We argue that prestigious directors can bring benefits as well as costs. We claim that the emergence of these costs depends on the institutional context, specifically the institutional characteristics of the country's corporate elite circle which is characterized by the elite cohesion and the elite exclusiveness. Our empirical results with a 15-country sample covering the period of 2005 to 2014 provide evidence for the overall existence of a positive performance effect of prestigious boards. However, our results also indicate that these beneficial effects of prestigious boards are mitigated in countries with high elite exclusiveness. Hence, under these certain institutional conditions, the elite-favouring behaviour of prestigious directors also brings costs.

Keywords: corporate elite, corporate governance, director network, institutions, prestigious directors

INTRODUCTION

The effect of board characteristics on firm performance has been a major focus of many studies in recent decades (Combs et al., 2007; Kor and Mahoney, 2005; Peng et al., 2003). The efficacy of directors' impact on firm performance is generally based on how the directors perform their board tasks, namely, providing advice and counsel (Forbes and Milliken, 1999; Hillman and Dalziel, 2003; Lynall et al., 2003), monitoring managers (Jensen and Zajac, 2004; Kroll et al., 2008; Mizruchi, 1983; Pearce and Zahra, 1991), and providing legitimacy in the factor and product markets (Hillman et al., 2007; Pfeffer and Salancik, 1978). The efficacy of directors usually depends on their human

and social capital or director capital in general because it affects the directors' capability to fulfil their monitoring role and/or to play a resource provision role (Hillman and Dalziel, 2003). Prestige of an individual director is one type of director capital that may have an important effect on firm performance.

Prestigious directors can benefit companies immensely as they provide legitimacy (Certo, 2003) and access to social capital (Boivie et al., 2012), and they can be a relevant source of power for the board of directors over the management (D'Aveni and Kesner, 1993). However, researchers have started questioning whether prestige can also be detrimental (Pollock et al., 2010) and have addressed the potential cost of prestigious directors (Acharya and Pollock, 2013). Prestigious directors form a country's economic or business elite, which is defined as the best or choice part of a larger group (The Concise Oxford Dictionary, 1990), or specifically, the choice part of the business community in this study. Often, corporate executives and board directors of large firms belong to this group, and we contend that the affiliation with these elites can influence the directors' behaviour. For example, such affiliation may lead to elite-favouring behaviour such as nepotism between directors and managers, which may mitigate directors' vigilant monitoring, although such behaviour is rarely in a company's best interest.

Researchers have shown that elite networks of directors shape countries' business systems (Scott, 1991; Useem, 1982) and often set the rules and shape the norms of the business world. The identification with the elite may cause them to behave in favour of the elite even at the expense of other stakeholders due to their motivation to support other elite members and/or to remain in this circle by conforming to the elite norms. At the same time, prestigious directors are endowed with rich director capital such as extensive social capital and access to valuable information and external resources, which can be leveraged for the firm's interests. Hence, the presence of prestigious directors on the board can be either detrimental or beneficial for the firm. We thus explore competing arguments to predict the performance implication of prestigious directors.

To disentangle the potential benefits and costs of prestigious directors and resolve the competing arguments, we introduce an institutional view on elites and treat some institutional factors as important contingencies. We argue that elite structures are societal phenomena that emerge at the institutional level and hence, our study also focuses on institutional-level characteristics that likely affect the efficacy of a country's elite. Our view is that the performance effect of prestigious directors is contingent upon the characteristics of elite structure, specifically the degree of elite cohesion and exclusiveness. When the cohesion of the elite is strong, i.e., elite members are concentrated among a small number of individuals, elite-specific norms and rules as well as proprietary information spread more effectively, as cohesive networks improve the consensus about the norms (Westphal and Khanna, 2003) and facilitate their diffusion (Davis et al., 2003). Such structures likely motivate prestigious directors to choose behaviours that preserve or enhance the benefits of the elite group sometimes at the expense of the focal firm's other stakeholders. Elite exclusiveness can lead to the formation of an elite group comprising of members from a similar social class background, which tends to lead to common understanding of appropriate behaviours and norms (Davis and Greve, 1997) that are sometimes distinct from those of external members of the elite circle. This exclusivity limits the diffusion of these norms beyond the elite's borders and thus may facilitate

unobserved behaviour that favours the elite group of prestigious directors. Thus, the exclusivity of the elites catalyses the implementation of the elite-specific rules and norms of prestigious directors. Both cohesion and exclusivity of the elite group, therefore, likely have negative moderating effects on the prestige–performance relationship.

By investigating these questions, our paper makes three important contributions. First, our study extends the concept of prestigious directors by adding the institutional lens. We discuss how institutional-level characteristics of elite structures, i.e., cohesion and exclusiveness, shape prestigious directors' behaviour and thereby affect the balance of costs and benefits of such directors. By connecting the firm-level effects of behaviour of prestigious directors to country-level institutional characteristics, we show how our research can provide deeper insight through the integration of the micro- and macro-level perspectives. Second, our study contributes to comparative corporate governance research. Prior studies examine the impact of board or director capital in single country contexts (e.g., Diestre et al., 2015; Haynes and Hillman, 2010; Tian et al., 2011). Our conjecture is that the effect of director capital likely varies by institutional context, as the way in which some dimensions of director capital influence directors' behaviour or firm outcomes is influenced by a local institution in which each director (and each board) is embedded. Third, we contribute to research on the effects of prestigious directors from a perspective of director capital. While prior board research examines the impact of various types of board capital, this study focuses solely on directors' prestige, thereby showing one of the key dimensions of director capital in depth.

The remainder of this paper is organized as follows. First, we discuss previous literature on the potential benefits and costs of prestigious directors. On the basis of this review, we develop two competing hypotheses regarding the overall performance effect of prestigious directors who have additional directorships or executive positions in large companies. Then we analyse the two institutional dimensions of the country-level elite structure that can affect the likelihood of these costs to be amplified. This is followed by a description of our data and methods and our empirical results. We conclude with a discussion on theoretical implications and a future research agenda.

THEORY AND HYPOTHESES

Previous research suggests that board capital has important implications on a firm's strategic behaviour (e.g., Haynes and Hillman, 2010; Oehmichen et al., 2017a, 2017b; Pugliese et al., 2009; Tuschke et al., 2013) and financial outcome (e.g., Johnson et al., 2013; Kor and Sundaramurthy, 2009; McDonald et al., 2008). According to Hillman and Dalziel (2003), board capital is the sum of individual director's human and social capital. While each individual directors have various experiences, expertise, and external ties that make up their own capital, prestige is one dimension that sets one director apart from other directors as it has many advantages, yet it is often difficult to obtain. The focus of this study is the performance impact of prestigious directors.

Prestige is based on the relationships and affiliations of corporate actors (Boivie et al., 2012). For example, the affiliation with prestigious parties is advantageous for firms as it enables them to gain the respect of, or simply impress, potential exchange partners in their environment, such as customers, investors, and other stakeholders (Chen et al.,

2008; Perrow, 1961; Pollock et al., 2010). Researchers have identified directors, in addition to top management team members (D'Aveni, 1990; D'Aveni and Kesner, 1993), as an important source of firm prestige (Certo et al., 2001). Directors are especially prestigious when they have sustainable personal relationships with important individual members in the firm's environment. However, how these prestigious[1] directors occupying board positions in large firms affect firm performance remains an open question.

Benefits of Prestigious Directors

Resource dependence theory offers several explanations for why prestigious directors have a positive performance effect. In order to carry out their advice and counsel function effectively, directors must have access to critical external resources (Hillman et al., 2007; Lynall et al., 2003). Such access is often facilitated by their relations to the external environment. Those external relations can be treated as the directors' social capital and prestige based on directorships and executive positions in important firms (Boivie et al., 2012). Ties to other important entities in a firm's external environment generate board social capital in the form of valuable relations to key stakeholders and industry incumbents, which allows the firm's management to access their resources (Adler and Kwon, 2002; Kor and Sundaramurthy, 2009; Tian et al., 2011). Ties to important firms ('high status' ties according to Shropshire, 2010, p. 254) are especially relevant for knowledge transfers through board members' additional directorships because the status increases the directors' ability and influence to diffuse knowledge (Shropshire, 2010). Hence, we argue that prestigious directors with directorships and executive positions in other large firms represent a critical resource channel for those directors to offer qualified advice and counsel, thereby positively affecting performance.

Additionally, prestigious directors have a considerable signalling effect (Acharya and Pollock, 2013; Certo et al., 2001) and also provide firms with important legitimacy (Certo, 2003). For instance, prior research has shown that prestigious directors are positively associated with higher IPO valuations (Pollock et al., 2010) and, accordingly, negatively associated with IPO underpricing (Certo et al., 2001). D'Aveni (1990) found a comparable signalling effect of prestige in his analysis of manager appointments, showing that firms appoint prestigious managers to prevent bankruptcy because such managers help to maintain the support of creditors. However, legitimacy is important not only for investors' or creditors' valuations but also for firms' relations with other key stakeholders, such as suppliers and customers (Hillman et al., 2008; Pfeffer and Salancik, 1978), as legitimacy sends a signal to those stakeholders that the firm is a reliable trading partner. In summary, the increased legitimacy acquired through prestigious directors increases a firm's success in capital and factor markets and thus has a positive effect on firm performance.

Besides enabling access to resources and legitimacy, prestige is an important source of power (D'Aveni and Kesner, 1993). For example, prestige is one of Finkelstein's (1992) power dimensions. He argued that 'an important source of power is personal prestige (or status)' (Finkelstein, 1992, p. 510). The power of directors likely has two effects. First, it increases the directors' external influence (relative to the power of the companies' stakeholders), and therewith, the firms' reputation and standing, and ultimately, the

firms' bargaining power in the market (Emerson, 1962; Pfeffer and Salancik, 1978). Second, it increases the directors' internal influence relative to the power of the CEO, allowing those directors to engage in more effective managerial monitoring (Combs et al., 2007). Pfeffer and Salancik (1978), for instance, argued that firms make use of powerful directors to buffer the effects of environmental uncertainties and to increase the exchange of information. Similarly, board members who are more powerful than the CEO can better influence the dismissal of underperforming CEOs (Flickinger et al., 2016) and the appointment process of future board members (Westphal and Zajac, 1995). Thus, with more prestigious directors, boards are able to fulfil their tasks more effectively, which, in turn, affects firm performance positively.

Based on these arguments, we propose our first hypothesis as follows:

Hypothesis 1a: Prestigious boards have a positive effect on firm performance.

Potential Cost of Prestigious Directors

While our discussion above focused on the positive effects of prestigious directors on firm performance, the presence of those directors may have some downsides. The research suggests that prestigious directors with directorships or executive positions in other large firms belong to an elite's inner circle (Acharya and Pollock, 2013; McDonald et al., 2008; Mills, 1956), and this affiliation can affect the directors' behaviour. Researchers have identified the following common behavioural patterns of elite members. First, the members of the elite group carefully guard their own status (Acharya and Pollock, 2013). Second, the elites tend to be subject to homosocial reproduction. Elite members use the power associated with their status to appoint directors who are similar to themselves (Westphal and Zajac, 1995; Zhu and Westphal, 2014), which could limit diversity within the elite circle. Once an individual has reached a high status position, he or she can more easily realize the advantages of additional high status positions and promotion (Benjamin and Podolny, 1999; Chen et al., 2008; Schaubroeck and Lam, 2002) because of the homophilous behaviour among elites; similar personal attributes have a strong influence on the appeal between individuals (McPherson and Smith-Lovin, 1987). Third, the research has shown that the members of an elite tend to help each other in both strategic (McDonald and Westphal, 2010) and personal matters (McDonald and Westphal, 2011). In short, prestigious directors may be motivated to act in the interests of other members in the elite circle and also share similar views with other elite members including executives, which can lead to a lack of diversity and potentially less innovative decisions.

These behavioural patterns can result in prestigious directors taking actions that are not necessarily in the interest of the firm or its stakeholders: they follow similar behavioural patterns, potentially stifling innovation or radical change, and hence they can potentially damage firm performance. For instance, prestigious directors might have close social ties to executives (Westphal and Khanna, 2003) and fear the loss of reputation and exclusion from the elite circles as a result of strictly monitoring these elite members (Westphal and Stern, 2007). In such a case, prestigious directors' monitoring of

executives may not be as strict and effective as the monitoring of non-prestigious directors. In order to support other elite members, including the CEO, prestigious directors may also bring in business practices through their interlocking board positions that benefit the CEO but not the shareholders. Due to the shared values and norms, those directors may not be able to challenge ineffective strategic proposals made by the CEO. In short, while board ties often facilitate the diffusion of new business practices, prestigious directors may be motivated to spread practices that are in the interests of executives and themselves. Indeed, prior studies show that social ties can result in less strictly bargained executive compensation contracts (Hwang and Kim, 2009; Westphal and Zajac, 1995), a higher probability of option backdating (Bizjak et al., 2009), and fewer CEO dismissals due to poor firm performance (Flickinger et al., 2016; Nguyen, 2012). Hence, having more prestigious directors on board reduces the boards' efficacy. Hence, we propose the following opposing hypothesis to Hypothesis 1a.

Hypothesis 1b: Prestigious boards have a negative effect on firm performance.

Although the potential positive effects of prestigious directors and their actions that reflect their elite favouritism at the expense of other stakeholders may co-exist in any institutional context, the extent to which such benefits or costs prevail may vary across institutional environments. We contend that relative effects are likely influenced by an institutional environment with certain characteristics. In the next section, we will shift the level of our analysis from the firm to the institutional level and examine how the institutional elite structure moderates the performance effects of prestigious directors.

Institutional-Level Elite Structure as a Moderator

The rules and norms of a society emanate from the institutional environment (DiMaggio and Powell, 1983). Institutions can influence firm behaviour by determining what is legitimate (Moore et al., 2012). Thus, institutions establish what are referred to as the 'rules of the game' (Moore et al., 2012; North, 1990; Peng et al., 2003; Wan and Hoskisson, 2003). Since elite members, including board directors, are embedded in a nation's institutional environment, it is expected that their behaviour will be affected by the institutional norms and rules. However, the institutional context varies by country. Interestingly, prior studies have already revealed that the efficacy of social capital varies across countries (Burt et al., 2000; Lin et al., 2009) and that institutions influence resource dependencies (Pfeffer and Salancik, 1978). Given these base arguments, to further our understanding of how directors with high prestige can affect firm performance in different country contexts, the institutional perspective must be integrated into our theoretical model. Additionally, the elite characteristics that affect the elite-favouring or self-serving behaviour of prestigious directors are a societal phenomenon. Therefore, we examine this phenomenon at the institutional level.

Our argument is that the elite structure in a country emanates from institutional characteristics that shape how these elite members relate to each other as well as to non-elite members and how these elite members are reproduced. We contend that the degrees of cohesiveness and exclusiveness of the elite circle are important contingencies that

influence their behaviour, which in turn affects the performance implications of prestigious directors. Specifically, we argue that greater degrees of elite cohesiveness and exclusiveness will negatively moderate the effect of prestigious directors on firm performance.

Elite cohesion. An efficient elite is characterized by a cohesive network of its members—also often called the 'small world' (Cohen et al., 2007; Nguyen, 2012). We contend that prestigious directors' behaviour and its effects are influenced by the extent of elite cohesion or the degree of concentration of corporate elite members, and that the impact of such behaviour could have important performance implications. We argue that directors' behaviours that serve the interests of the elite are facilitated when the elite members closely share norms and interests and can easily reach a consensus about these norms within a small circle of elite members. Prestigious directors in countries with such cohesive elite structures are likely better informed about the elite norms and interests as the dense network of directors represents an efficient information channel. The members of a cohesive elite meet often and can share their worldviews and observe their codes of honour (Davis et al., 2003; Mills, 1956).

Prestigious directors' behaviour is likely influenced by cohesive elites not only because they share elite-specific rules and norms but also because their deviant behaviour would likely be more easily detected by other members in a small cohesive circle, which may lead to social sanction. For example, in cases of defection from the rules of the elite, the elites use social distancing to punish non-compliant members (Westphal and Khanna, 2003). Social distancing in the case of directors includes 'acts of avoidance and snubbing as neglecting to invite directors to informal board meetings, not asking their opinion or advice in formal meetings, not acknowledging or building on their comments in discussion, and engaging in exclusionary gossip whereby board members talk about other people and events with which the focal director is not familiar' (Westphal and Khanna, 2003, p. 365). Although prestigious directors may face fewer sanctions for deviation from the elite norms than less prestigious directors (He and Huang, 2011; Westphal and Khanna, 2003), a cohesive elite structure likely mitigates this tendency since greater cohesion means fewer opportunities for a deviant director to obtain other elite positions due to the small world structure.

This elite cohesion among directors often emerges through individual directors occupying multiple directorates in different firms and the resulting ties between individual directors (Mizruchi, 1996). Several studies have indicated that different kinds of business practices are diffused across firms through networks created by shared directorates (Bizjak et al., 2009; Davis, 1991; Davis and Greve, 1997; Haunschild, 1993). For example, Haunschild (1993) showed that directors imitate the practices of other firms when they sit on those firms' boards. More specifically, Davis and Greve (1997) found that directors use their social networks to spread business practices such as poison pills. Similarly, Bizjak et al. (2009) showed that the practice of option backdating could also spread through the director network. Thus, these prior studies indicate that the normative understanding of business practices spreads through the director network, and the diffusion is likely more efficient in a dense network.

Greater elite cohesion can have negative effects on the performance impact of prestigious directors. When elite members are connected in a highly cohesive elite structure,

they are likely to be able to share elite norms and behavioural expectations more efficiently. As discussed earlier, due to the fear of exclusion from the elite circle, prestigious directors are unlikely to attempt to intensively monitor senior executives, who usually belong to the same elite circle. This tendency can be amplified in a small circle due to more efficient information flow and limited opportunities for other elite positions. This implies that executives of even poorly performing firms may not receive much scrutiny or punishment from the board. Further, those directors may be willing to accept business practices that favour elite members even at the expense of shareholders and other stakeholders because of their incentives to advance the elite members' interests and also to avoid social exclusion. For example, members of the cohesive elite might be willing to support stock option backdating for executive compensation packages because they have become used to this practice within their elite network.

While such elite-favouring behaviour may have a negative performance impact because prestigious directors do not engage in managerial monitoring and rather facilitate the diffusion of business practices that could damage the interests of shareholders and stakeholders, we could argue that such behaviour might lead to a positive performance effect when those directors' motive to support other elite members is aligned with the firm's and shareholders' interests. In addition to managerial monitoring, directors often engage in providing resources that are valuable to the focal firm (Hillman and Dalziel, 2003). Prestigious directors' incentives to conform to the elite norms in a small elite circle, thereby supporting executives who also belong to the same circle, can also facilitate their resource provision role as a board member. For example, when the CEO of the focal firm is facing pressure from shareholders to improve firm performance, prestigious directors in an environment characterized by cohesive elite structures may be more willing to play a resource provision role by giving advice to the CEO and/or bringing in external resources that help improve firm performance (McDonald and Westphal, 2010). Therefore, the elites' incentives to support each other may positively impact performance.

However, such positive effects are likely to be realized only under specific conditions, e.g., when CEOs are facing pressures from investors or competitors who do not share the same elite norms. Even then, it is possible that elite members can support each other by finding ways to evade such pressures, e.g., by working with affiliated block shareholders or friendly firms to dampen pressure from arm's-length investors or competitors, rather than directly responding to the market demands. Hence, prestigious directors' resource provision may not always have performance enhancing effects.

In summary, we argue that a cohesive elite network likely enhances the potentially negative performance effects of prestigious directors. Due to strong and clear elite-specific norms and the threat of social punishment, prestigious directors in these countries have a stronger motivation to act in favour of the elite, which may likely end up hurting the interests of the firm's other stakeholders. Therefore, we have the following hypothesis:

Hypothesis 2: The cohesion of the corporate elite has a negative effect on the relationship between prestigious boards and firm performance.

Elite exclusiveness. Another institutional-level factor that can influence the impact of prestigious directors on firm performance is elite exclusiveness. While the elite cohesion affects directors' behaviour through their interactions or relationships with other members in a small elite circle, elite exclusiveness influences their behaviour not only through their relationships with other elite members but also through their relationships with external groups or individuals outside the elite circle. Being exclusive implies having a clear distinction between in-group members and others. The more exclusive a country's elite circle is, the better its members can keep their behaviour private from the scrutiny of non-members outside the circle. While the elite tends to create its own normative understanding of business practices, such elite-specific norms and best practice rules can persist in exclusive elite structures because the boundary between the elite and external world is not very porous when the extent of exclusiveness is high. As a result, the out-group members can neither observe nor mimic these practices easily; in other words, elite members can determine within their inner circle which behaviour is appropriate (Davis and Greve, 1997). This exclusivity also defends them from any institutional mimicking of their norms (DiMaggio and Powell, 1983) and thus protects the stability of the elite structure.

We argue that countries' elites can protect their exclusiveness by allowing as little mobility between social classes as possible. In this way, the members of the elite always belong to the same social class. The similar social class background benefits the information flow among the elite members. Researchers who have examined the aspect of information flows within the small world phenomenon have shown that greater social distance can restrict social communication (Milgram, 1967). Within a corporate governance context, this means that contacts from similar social settings are particularly influential in 'transporting' business practices (Davis and Greve, 1997).

Allowing as little social mobility as possible is achieved through the homosocial reproduction in the elite. This line of argumentation follows Bourdieu's theory of the reproduction of social class structures, according to which class-specific habitus stabilizes social structures (Hartmann, 2000). Thus, elite exclusivity can be seen as the institutional-level equivalent of homophilous behaviour based on status (Chen et al., 2008; McPherson and Smith-Lovin, 1987). However, whereas status (or prestige) is a situation-specific attribute (Gray and Kish-Gephart, 2013) that describes an individual's role in the business context, the reproduction of the social class represents an exogenous process at the country level that nevertheless can have a moderating effect on firm-level outcomes, such as the relationship between prestigious directors and firm performance.

We argue that in institutional contexts where social class reproduction is prevalent the elite-favouring behaviour of prestigious directors is facilitated because the directors can be assured that information regarding their behaviour will not easily leak out of the elite circle. In such an institutional context, directors know that the individuals whom they meet in similar hierarchical positions, more specifically in the boardroom, come from a similar social class background (Gray and Kish-Gephart, 2013), which tends to lead to a favourable view of each other based on homophily. Such an interpersonal relationship can easily generate a common normative understanding of business practices (Davis and Greve, 1997) and facilitate the behaviour in favour of the elite. This also amplifies homogeneity or a lack of diversity among the elite members, which can lead to

less innovative decisions. Some of such behaviour can be detrimental to the interests of a firm and its shareholders. Prestigious directors may simply ignore their monitoring responsibility since they have a cordial relationship with the CEO due to their shared social background. They may also support business practices that advance the CEO's and their own interests, as they can prioritize in-group members' interests more than out-group members' due to the low risk of being detected. Those directors may simply conform to the view of the elite members because they perceive issues from a similar viewpoint. When the elite exclusivity leads to such behaviour that ignores the interests of other stakeholders, it will likely negatively moderate the effect of prestigious directors on firm performance.

However, the elite members in an institutional environment with greater elite exclusivity may need to maintain legitimacy in the eyes of stakeholders and the public since there are sometimes tensions between exclusivity and legitimacy (Ashley et al., 2015; Powell, 1988). To retain exclusivity, the elite members need to limit mobility between social classes, and yet they may also have to get others in society to accept, at least to some extent, that this distinction as legitimate. At the macro level, for example, Yue and colleagues (2013) show that the failure of the banking industry in New York through the elite's attempt to privately regulate the industry led to a loss in legitimacy, harming the elite's interests. At the firm level, those directors may face pressure to show their value in contributing to the goals of the firm, of which financial performance is critical to remaining legitimate in the eyes of investors.

However, being exclusive implies that people in the general public do not have much information about how those members who belong to this exclusive circle behave and hence, those elite members may not feel much pressure to show legitimacy. After all, as such elite circle is an informal group where members are not necessarily selected based on their ability to contribute to firm performance, its members may not feel much pressure to justify their exclusiveness. Therefore, our last hypothesis is as follows:

Hypothesis 3: The exclusiveness of the corporate elite has a negative effect on the relationship between prestigious boards and firm performance.

METHODS

Sample and Data Sources

The sample includes all firms listed in the S&P500 and FTSE350 as well as all listed firms from 13 continental European countries included in the BoardEx database between 2005 and 2014. This time frame has the advantage that it includes times of economic upswing until 2007 as well as the economic downswing due to the financial crisis. Thus, the time frame represents a complete economic cycle, and hence it enhances the generalizability of our results. In total, it encompasses 1918 firms from 15 countries: Belgium, Switzerland, Germany, Denmark, Spain, Finland, France, Greece, Ireland, Italy, the Netherlands, Norway, Sweden, the UK, and the USA. We chose those European countries because they had at least one company included in the MSCI

Europe index in our time frame. We excluded Austria due to limited data availability in the BoardEx database for the years 2005 and 2006 and Portugal due to limited data availability in 2013 and 2014. We restricted the sample to the S&P500 and FTSE350 because in the USA and the UK – in contrast to the other countries in our sample – very small firms are publicly listed; therefore, including all of them in the sample would create a sample selection bias in general, as well as a large country bias in the moderation analyses. Further, we excluded financial services firms due to their specific balance sheet structure. The firm-level data were collected from Worldscope. The individual-level information on board members was obtained from BoardEx. For greater comparability across the different corporate governance systems in our sample, and due to our study's focus on the supervisory function of the board, we excluded all executive board members[2] and employee representatives on the board. We used BoardEx data from 2001 to 2014 because the prestige measure takes into account a 5-year experience of every director (e.g., prestigious directors in 2005 were calculated based on individual director information from 2001 to 2005, and prestigious directors in 2014 were based on director information from 2010 to 2014).

We started with a sample of 3136 publicly listed firms in the BoardEx database, with at least 2 firm years available in our time frame from 2005 to 2014. After excluding financial companies, 2447 firms were left. Further observations were dropped due to lagging variables and because we applied list-wise deletion when at least one variable was not available. Consequently, we ended up with 13,185 firm years in 1918 companies for our analysis.

Measures

Prestigious directors. A measure for prestigious directors is not easy to build across different countries with specific cultures and corporate governance systems. As we have argued above, prestigious directors have specific effects on organizational outcomes since they represent a special subgroup among the supervisory directors in a country. Generally, prestige can arise out of different areas. Acharya and Pollock (2013) identify a degree from an elite educational institution, experience as an executive at an S&P500 firm, and experience as a supervisory director at an S&P500 firm for their analysis of US companies. Since we are investigating elites in different countries, these measures cannot easily be used for cross-country comparisons. For a multi-country analysis, it is not possible to identify comparable elitist educational structures. While countries like the S or France have a distinguished group of elitist universities with prestigious names, for most other countries in our sample the best education can be found in many different universities, and there is no such clear prestige for having graduated from a specific institution. Additionally, in other countries such as the UK elite education is not limited to the university level but starts earlier with elitist boarding schools. Hence, in a multi-country study it is hard to capture elite education with a comparable measure. We therefore did not include such a measure to capture prestige, focusing instead on the prestige that individuals accumulate during their working life and excluding educational prestige from our measure.

Focusing on their professional background, we operationalize the construct of prestigious directors on the board by identifying those directors with the highest cumulative influence. We refrain from basing our measure on the membership in a stock index since these indices are heterogeneous in size and relevance across the countries in our sample. Instead, we measure this cumulative influence by aggregating the logarithm of the market value of the firms in the respective country (cross-country directorships are extremely rare and are neglected without causing much error) in which a director has held a board-level position (executive and supervisory) in the past five years (as explained above, for board prestige in 2005, e.g., we used director positions from 2001 to 2005; for the 2014 measure, we used 2010 to 2014 positions). In doing this, we obtain a ranked list for all directors (persons, not positions) that hold a directorship in at least one company of our sample in a specific year. To do so, we had to merge BoardEx data with the financial firm-level data from Worldscope. Directors without directorships with the market value available on Worldscope were excluded from the ranking. The company and director sample available through the BoardEx database for the years 2005 to 2014 covers an average of 89 per cent of the market capitalization of all listed companies in the sample countries (Adams and Kirchmaier, 2012), with mostly small companies absent. Therefore, we conclude that the dataset is appropriate for the operationalization of our constructs. To construct the final measure for the regression analysis comparable across countries, we identify the top tercile (results are robust using the top quartile instead – for more details, see the robustness section) of the directors on the resulting list as prestigious because we assume that these directors represent the most influential and therefore most prestigious individuals in the group of supervisory directors in a country. The company-level variable used in the regression analysis is the percentage of such identified prestigious directors on the board.

Institutional elite characteristics. We test the contingency effect of the two institutional elite characteristics: cohesion and exclusiveness. For elite cohesion, we refer to the network of directors who occupy board positions in multiple companies. The cohesion of a country's corporate elite network is approximated by the concentration of this network. To capture this concentration, we measure the density of country's corporate elite network. We measure this by counting all existing ties in the network and normalizing this number by dividing the resulting value by the number of all possible ties in the network (the number of all possible ties equals $(n-1)*(n-2)/2$). To use the variable in our panel data design, we must make the variables comparable across years. Hence, we standardize the resulting values to a [0, 1] interval, where 0 represents the lowest and 1 the highest density in a specific year. This means that the value 0 for Italy indicates that Italy is the country with the least coherent network, whereas the value of 1 for Ireland indicates the highest cohesion. One concern with this approach is that the density measures are not necessarily comparable between countries since the number of possible ties increases with the square of the number of nodes, while likely assumptions for the number of actual ties in the network would assume more or less linear growth with network size. To address this concern, we used subsamples of the 40 largest companies by market value for each country to calculate the density measures on roughly the same network size, thereby accounting for the limited

Table Ia.   Elite cohesion measure (standardized)

Country	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014
Belgium	0.26	0.31	0.39	0.31	0.34	0.26	0.18	0.23	0.24	0.14
Switzerland	0.06	0.09	0.13	0.16	0.14	0.16	0.28	0.19	0.14	0.15
Germany	1.00	1.00	1.00	1.00	1.00	0.94	1.00	0.89	1.00	1.00
Denmark	0.31	0.30	0.29	0.28	0.29	0.29	0.20	0.29	0.25	0.40
Spain	0.23	0.28	0.24	0.41	0.41	0.34	0.40	0.35	0.44	0.19
Finland	0.30	0.30	0.27	0.26	0.26	0.32	0.32	0.31	0.29	0.35
France	0.64	0.78	0.88	0.85	0.86	0.82	0.84	1.00	0.65	0.44
Greece	0.09	0.11	0.23	0.30	0.39	0.29	0.30	0.35	0.24	0.44
Ireland	0.01	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.13
Italy	0.50	0.44	0.48	0.40	0.46	0.53	0.30	0.62	0.45	0.00
Netherlands	0.23	0.19	0.19	0.25	0.19	0.25	0.11	0.23	0.23	0.28
Norway	0.00	0.03	0.04	0.04	0.06	0.05	0.06	0.07	0.04	0.15
Sweden	0.64	0.61	0.69	0.89	0.88	1.00	0.97	0.93	0.64	0.62
United Kingdom	0.15	0.22	0.25	0.36	0.26	0.30	0.26	0.26	0.24	0.38
United States	0.20	0.17	0.20	0.26	0.29	0.22	0.20	0.33	0.28	0.25

Notes: Elite cohesion measures (standardized) for the countries in our sample.

number of companies in the smaller countries, while simultaneously maximizing the representativeness of the sample. However, for robustness, we also estimated our models with alternative subsample sizes (35 and 45 companies). The final (standardized) ELITE COHESION values for the different countries as well as unstandardized values are displayed in Tables Ia and b.

Table Ib.   Elite cohesion measure (unstandardized)

Country	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014
Belgium	0.05	0.05	0.05	0.04	0.04	0.03	0.02	0.02	0.03	0.01
Switzerland	0.02	0.02	0.02	0.02	0.02	0.02	0.03	0.02	0.02	0.01
Germany	0.14	0.13	0.12	0.10	0.10	0.10	0.09	0.08	0.10	0.05
Denmark	0.05	0.05	0.04	0.03	0.03	0.03	0.03	0.03	0.03	0.03
Spain	0.04	0.04	0.03	0.05	0.04	0.04	0.04	0.03	0.05	0.02
Finland	0.05	0.05	0.04	0.03	0.03	0.04	0.04	0.03	0.03	0.02
France	0.10	0.10	0.10	0.09	0.09	0.08	0.08	0.09	0.06	0.03
Greece	0.03	0.02	0.03	0.04	0.04	0.03	0.03	0.03	0.03	0.03
Ireland	0.01	0.01	0.01	0.01	0.01	0.00	0.01	0.00	0.01	0.01
Italy	0.08	0.06	0.06	0.04	0.05	0.06	0.03	0.06	0.05	0.01
Netherlands	0.04	0.03	0.03	0.03	0.02	0.03	0.02	0.02	0.03	0.02
Norway	0.01	0.01	0.01	0.01	0.01	0.01	0.01	0.01	0.01	0.01
Sweden	0.10	0.08	0.08	0.09	0.09	0.10	0.09	0.08	0.06	0.04
United Kingdom	0.03	0.04	0.04	0.04	0.03	0.03	0.03	0.03	0.03	0.02
United States	0.04	0.03	0.03	0.03	0.03	0.02	0.02	0.03	0.03	0.02

Notes: Elite cohesion measures (unstandardized) for the countries in our sample.

Table IIa. Elite exclusive measure (standardized)

Country	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014
Belgium	0.81	0.76	0.64	0.18	0.54	1.00	0.18	0.19	0.51	0.26
Switzerland	0.92	0.96	0.96	0.22	0.54	0.00	0.32	0.68	0.15	0.66
Germany	1.00	0.99	1.00	0.30	0.27	0.28	0.60	0.50	0.73	0.91
Denmark	0.54	0.62	0.97	1.00	1.00	0.70	0.45	1.00	1.00	0.90
Spain	0.71	0.60	0.79	0.44	0.44	0.37	0.30	0.39	0.19	0.40
Finland	0.00	0.62	0.69	0.96	0.88	0.46	0.69	0.74	0.92	0.86
France	0.55	0.00	0.62	0.12	0.00	0.33	1.00	0.39	0.20	0.48
Greece	0.70	0.96	0.00	0.09	0.32	0.70	0.50	0.64	0.26	0.67
Ireland	0.99	1.00	0.88	0.47	0.04	0.64	0.65	0.35	0.59	0.37
Italy	0.65	0.67	0.30	0.43	0.42	0.35	0.25	0.02	0.00	0.00
Netherlands	0.70	0.39	0.57	0.25	0.27	0.15	0.43	0.39	0.51	0.68
Norway	0.85	0.87	0.63	0.04	0.34	0.03	0.17	0.35	0.09	0.01
Sweden	0.95	0.65	0.84	0.00	0.35	0.48	0.52	0.27	0.45	0.62
United Kingdom	0.82	0.72	0.63	0.67	0.46	0.33	0.42	0.36	0.44	1.00
United States	0.81	0.74	0.63	0.05	0.15	0.15	0.00	0.00	0.37	0.36

Notes: Elite exclusive measures (standardized) for the countries in our sample.

To quantify the exclusiveness of the corporate elite circle in a country, we measured the permeability of the elite circle. To do this, we used the list of prestigious directors as described above and calculated for each country the percentage of directors in the elite group that were already in the elite the year before. This value measures how difficult it is for new individuals to join the elite and therefore the exclusiveness of the elite circle. The measure is standardized in the same way as elite cohesion. The final ELITE EXCLU-SIVENESS values for the different countries as well as unstandardized values are displayed in Tables IIa and b. As a robustness test for this measure, we used a social mobility indicator from the OECD. This intergenerational social mobility measure from the OECD 'Education at a Glance' study represents the participation in higher education of students whose parents have low levels of education (OECD, 2012). The inverse of this measure is a proxy for elite exclusiveness because it reveals the degree of change in the composition of the upper social classes in a more general way at the level of society.

Measurement of Performance and Control Variables

Measures of firm performance. In our analysis, we focus on firm operating performance, which is approximated by the return on assets (ROA). We calculate ROA as earnings before interest and tax, divided by total firm assets. This measurement has been used previously for multi-country analyses since it is not influenced by a country's tax regime or a firm's capital structure (Crossland and Chen, 2013; Defond and Hung, 2004). Since our sample is based on the years 2005 to 2014 and follows a panel data design, we used the performance measure for the respective years from 2005 to 2014.

Board characteristics. We controlled for board characteristics in our analysis. BOARD SIZE is measured as the number of supervisory directors on a board. For reasons of comparability

Table IIb. Elite exclusive measure (unstandardized)

Country	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014
Belgium	0.75	0.74	0.72	0.72	0.78	0.81	0.66	0.66	0.73	0.42
Switzerland	0.79	0.77	0.81	0.73	0.79	0.69	0.68	0.75	0.65	0.59
Germany	0.82	0.78	0.82	0.74	0.72	0.72	0.74	0.72	0.78	0.70
Denmark	0.66	0.72	0.81	0.85	0.90	0.77	0.71	0.81	0.83	0.69
Spain	0.72	0.72	0.76	0.76	0.76	0.73	0.68	0.70	0.66	0.48
Finland	0.48	0.72	0.73	0.84	0.87	0.74	0.75	0.76	0.82	0.67
France	0.67	0.63	0.71	0.71	0.65	0.73	0.81	0.70	0.66	0.52
Greece	0.72	0.78	0.55	0.71	0.73	0.77	0.72	0.75	0.68	0.59
Ireland	0.82	0.78	0.78	0.77	0.66	0.77	0.74	0.69	0.75	0.47
Italy	0.70	0.73	0.63	0.76	0.76	0.73	0.67	0.63	0.62	0.32
Netherlands	0.72	0.69	0.70	0.73	0.72	0.71	0.70	0.70	0.73	0.60
Norway	0.77	0.76	0.72	0.70	0.74	0.69	0.66	0.69	0.64	0.32
Sweden	0.80	0.73	0.77	0.69	0.74	0.75	0.72	0.68	0.72	0.58
United Kingdom	0.76	0.74	0.72	0.80	0.76	0.73	0.70	0.69	0.71	0.73
United States	0.75	0.74	0.72	0.70	0.69	0.71	0.63	0.63	0.70	0.47

Notes: Elite exclusive measures (unstandardized) for the countries in our sample.

between countries, we excluded employee representatives from this measure. We controlled for the PERCENTAGE OF OUTSIDE directors as an independence measure applicable to multi-country analyses. Outside board members are hereby defined as board members who did not work for the company before their appointment to the supervisory role. FEMALE DIRECTORS is defined as the percentage of women among the board members and used as a control for effects of board gender diversity. CEO TIR (time in role) is defined as the time that the CEO has been working as the chief executive of the company. Furthermore, we controlled for CEO PRESTIGE, which we measured in line with the prestigious director measure as a logarithm of the aggregated market value of CEOs' board-level position (executive and supervisory) in the past five years. The variable BUSYNESS controls for the downside effects of multiple directorates that have been shown to affect business performance when too many board members are limited in the time available for their supervisory function (Boivie et al., 2012). Consistent with prior studies, we define this as the percentage of directors with three or more directorates (Fich and Shivdasani, 2006).

Measures of ownership structures. We controlled for the effects of different ownership structures in terms of the influence of institutional investors and the effect of large blockholders in general. The variable INSTITUTIONAL INVESTORS measures the number of large institutional owners. We hereby count investors as large when they hold more than ten percent of a company's shares. The variable PERCENTAGE LARGE OWNERS indicates the percentage of shares held by the ten largest owners in a company.

Firm characteristics. Several firm characteristics serve as additional control variables in our analysis. We controlled for effects of prior firm performance using ROA lagged by one year. To control for the different outcomes of firms of different sizes, we include FIRM

SIZE as the natural logarithm of a firm's total assets. The variable FIRM RISK is the standard deviation of the return on equity in the past three years, divided by the mean return on equity in the past three years. This controls for the volatility in a firm's performance outcomes. SALES CHANGE measures the difference in total sales over one year and controls for disruptions in firm output influencing company performance. To control for different financial structures, we include LEVERAGE, calculated as the ratio of long-term debt to total capital. We accounted for firm DIVERSIFICATION with an entropy measure as suggested, for example, by Palepu (1985). It is measured as $\sum p_{ij} * \ln\left(1/p_{ij}\right)$, where p_{ij} is the proportion of a firm i's sales in business segment j and $\ln\left(1/p_{ij}\right)$ is the weight of each segment j. This measure controls for the effects of a company's scope on its performance. Additionally, we controlled for firm prestige using a dummy variable that indicates whether the firm was listed in the prestigious indices S&P100 or MSCI Europe for the respective year.

To incorporate industry effects within our regression models, we used two-digit SIC code dummies. Year dummies are included in the estimation to control for year-specific effects. Country dummies are included to control for those country effects that are not captured by the moderator variables. Table III summarizes the descriptive statistics and pairwise correlations for the variables used in the analysis.

EMPIRICAL ANALYSIS

Empirical Strategy

We used a longitudinal dataset for the analysis, spanning the years 2005 to 2014. The main objective of this study is to analyse the effect of prestigious directors on a firm's performance and the influence of the institutional setting on this relationship. To examine this relation empirically, we analysed variants of the following model specification:

PERFORMANCE = f(average number of prestigious directors, moderators, interaction terms, board controls, ownership controls, and firm controls)

Our data depict a 'small T, large N' situation with few time periods and many firms for which we assume the presence of fixed effects as well as heteroskedasticity and autocorrelation within firms, but not across them. Additionally, the dependent variable and some independent variables are not strictly exogenous; they are correlated with past and possibly current realizations of the error term. Including such variables in a standard fixed-effects equation is problematic due to the high probability that the error term will be correlated with the lagged endogenous variable. Consequently, we adopted the system GMM estimator proposed by Arellano and Bover (1995) and Blundell and Bond (1998) for our analysis. This approach has recently been used in several studies with comparable research designs (Cheng et al., 2014; He and Huang, 2011; Wade et al., 2006). For our estimations, we employed the xtabond2 module in Stata 14 (Roodman, 2009).

The GMM estimator reduces potential problems regarding endogeneity as it is based on instrumental variables estimation using the lags of the variables as estimators, simultaneously allowing the use of the lags of the dependent variable (Roodman, 2009). Additionally, it controls for firm-specific heteroskedasticity using orthogonal conditions and

Table III. Means, standard deviations, and correlations

	Mean	S.D.	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)	(14)	(15)	(16)	(17)	(18)	(19)	(20)	(21)
(1) Return on assets	8.29	10.90	1.00																				
(2) % prestigious directors	0.31	0.38	0.08*	1.00																			
(3) Elite cohesion	0.41	0.29	−0.1*	−0.03*	1.00																		
(4) Elite exclusiven.	0.45	0.30	0.05*	0.00	0.02	1.00																	
(5) Interaction term1	0.01	0.19	0.06*	0.81*	−0.01	0.01	1.00																
(6) Interaction term2	0.01	0.20	0.06*	0.84*	−0.02*	0.02*	0.69*	1.00															
(7) Board size	1.94	0.45	0.05*	0.31*	−0.09*	−0.14*	0.31*	0.27*	1.00														
(8) Busyness	0.24	0.21	0.07*	0.32*	−0.15*	0.00	0.36*	0.27*	0.25*	1.00													
(9) % outsiders	0.77	0.19	0.02*	0.05*	−0.04*	−0.08*	0.03	0.05*	0.20*	0.03*	1.00												
(10) Female directors	0.14	0.13	0.06*	0.13*	−0.03*	−0.10*	0.09*	0.12*	0.12*	0.10*	0.10*	1.00											
(11) CEO duality	0.32	0.47	0.03*	0.03*	−0.08*	−0.17*	0.00	0.01	0.19*	0.05*	0.20*	0.14*	1.00										
(12) CEO time in role	5.55	5.64	0.05*	−0.06*	0.10*	0.00	−0.07*	−0.06*	−0.16*	−0.09*	−0.03*	0.02*	0.12*	1.00									
(13) CEO prestige	−1.35	8.63	−0.01	0.28*	0.01	−0.10*	0.25*	0.23*	0.17*	0.15*	0.06*	0.09*	0.14*	0.02*	1.00								
(14) Blockholder	0.49	0.20	−0.03*	−0.26*	0.23*	−0.02*	−0.23*	−0.21*	−0.20*	−0.25*	−0.01	−0.09*	−0.07*	0.10*	−0.11*	1.00							
(15) Institutional inv.	0.33	0.60	−0.06*	−0.13*	−0.10*	0.04*	−0.08*	−0.11*	−0.12*	0.05*	−0.05*	−0.02*	−0.05*	−0.04*	−0.02*	0.22*	1.00						
(16) Firm size	14.74	1.80	0.13*	0.56*	−0.12*	−0.13*	0.54*	0.49*	0.64*	0.38*	0.17*	0.18*	0.20*	−0.11*	0.21*	−0.31*	−0.16*	1.00					
(17) Company prestige	0.23	0.42	0.10*	0.41*	−0.01	0.09*	0.33*	0.34*	0.21*	0.21*	0.01	−0.06*	−0.02*	−0.05*	0.11*	−0.18*	−0.09*	0.36*	1.00				
(18) Leverage	0.20	0.16	−0.10*	0.08*	−0.11*	−0.07*	0.08*	0.08*	0.18*	0.06*	0.07*	0.04*	0.06*	−0.07*	0.05*	−0.06*	0.02*	0.23*	0.05*	1.00			
(19) Total diversific.	0.31	0.41	0.01	0.15*	0.05*	0.06*	0.13*	0.13*	0.13*	0.07*	−0.01	−0.01	0.01	0.02*	0.07*	−0.07*	−0.07*	0.19*	0.16*	−0.01	1.00		
(20) Firm risk	0.24	2.50	0.05*	0.01	0.01	0.01	0.01	0.01	0.01	0.01	−0.01	0.00	−0.01	0.01	−0.01	−0.01	−0.02	0.03*	0.02*	0.01	0.02*	1.00	
(21) Salesgrowth	0.08	0.26	0.14*	−0.04*	−0.02*	0.07*	−0.04*	−0.05*	−0.05*	−0.05*	0.00	−0.07*	0.00	0.02*	−0.09*	0.00	−0.01	−0.04*	−0.02	−0.02*	−0.05*	0.02*	1.00

Notes: n = 13,185; significance levels: *p < 0.05.

provides better estimates in the presence of autocorrelation, as compared to fixed effects models. We used a two-step system GMM estimator because one-step estimators may produce biased estimates when variables vary little over time (Arellano and Bover, 1995; Blundell and Bond, 1998). We applied Windmeijer-corrected standard errors to control for downward bias in the estimator (Windmeijer, 2005).

Additionally, we report diagnostic tests to confirm estimation validity. The Arellano–Bond test (AB-test) for the first-order autocorrelation of disturbances should indicate significant first-order serial correlation from GMM's first-differenced estimation (Arellano and Bond, 1991). The second order test should be free of autocorrelation and give a non-significant result. A chi-square test checks potential model misspecification and confirms the model's explanatory power (Hair et al., 2006). The Sargan/Hansen test for over-identifying restrictions tests for the independence of the instruments from the error term. We provide Hansen's J statistics instead of the Sargan test because the Sargan statistic can become inconsistent with the use of Windmeijer-corrected standard errors (Roodman, 2009). In all our models, the results suggest that the model is well-fitted (chi-square < 0.001) and appropriate for use with system GMM (significant first-order AB-test and non-significant second order AB-test and Hansen's J statistic).

Empirical Results

Table IV provides the regression analysis results on the relationship between the average number of prestigious directors and firm performance. The dependent variable is the ROA. Model 1 shows the regression results for the main effect. It includes all the control variables and the average number of prestigious directors as independent variables. The influence of the average number of prestigious directors on firm performance is significant and positive ($p < 0.01$), thus supporting Hypothesis 1a but rejecting Hypothesis 1b. This confirms the general idea that firms benefit from prestigious directors on their boards; they bring advantages that outweigh the potential negative effects. The result also suggests that prestigious directors do not engage in behaviours that benefit themselves at the expense of the interests of the firm and shareholders. Our multi-country sample supports the assumption that this is generally true for different countries.

Model 2 extends the main model with the elite cohesion variable and its interaction with prestigious directors. Hypothesis 2 predicts a negative effect of the cohesion of a country's elite on the relationship of prestigious directors and company performance. As Model 2 shows, the interaction is indeed negative. However, the effect is not significant. Hence, model 2 does not support Hypothesis 2. The negative effect of a cohesive network on the relationship between prestigious directors and firm performance might be accompanied by a positive effect as directors with multiple board positions can also transfer positive business practices with potentially positive effects more efficiently in dense networks. Examples of those positive practices could be a quality control practice or efficient business process system, from other firms where they serve as a board member in order to support the CEO. Such behaviour can also send a positive signal about the director within a small elite circle as being a valuable member. Model 3 tests Hypothesis 3 which predicts that a high exclusiveness of countries' elite circles will decrease the

Table IV. Regression results

Dependent variable	Model 1 ROA		Model 2 ROA		Model 3 ROA	
	Coeff.	S.E.	Coeff.	S.E.	Coeff.	S.E.
% prestigious directors	5.77**	(1.82)	4.76*	(2.41)	6.03**	(1.87)
Elite cohesion			0.65	(1.30)		
% prestigious directors * elite cohesion			−2.13	(3.16)		
Elite exclusiveness					0.33	(0.39)
% prestigious directors *elite exclusiveness					−2.66*	(1.05)
Board characteristics						
Board size	−2.47	(1.99)	−1.37	(2.00)	−0.58	(2.04)
Busyness	−0.14	(1.24)	0.44	(1.26)	−1.51	(1.81)
% outsider	1.96	(2.40)	3.97	(2.44)	1.25	(2.41)
Female directors	2.77	(2.98)	4.75	(3.04)	2.54	(2.95)
CEO Duality	0.21	(1.12)	1.30	(1.08)	1.17	(1.05)
CEO TIR	−0.08	(0.07)	−0.09	(0.07)	−0.03	(0.07)
CEO prestige	−0.15**	(0.06)	−0.06	(0.06)	−0.09	(0.06)
Ownership characteristics						
Blockholder	−2.39	(3.22)	−3.14	(3.45)	−0.38	(3.32)
Institutional invt	−0.37	(0.75)	−0.36	(0.80)	−1.18	(0.80)
Firm characteristics						
ROA_{t-1}	0.55***	(0.05)	0.60***	(0.05)	0.49***	(0.05)
Size	−1.01	(0.71)	−0.72	(0.58)	−0.84	(0.68)
Company prestige	0.45	(0.49)	0.16	(0.51)	0.30	(0.50)
Leverage	9.39*	(4.35)	15.94***	(4.69)	9.22*	(4.33)
Diversification	−0.75	(0.99)	−0.89	(1.02)	−0.04	(0.98)
Risk	−0.44	(0.33)	−0.39	(0.36)	−0.57[†]	(0.34)
Salesgrowth	6.53***	(1.77)	3.95*	(1.95)	4.91*	(2.07)
Constant	65.70*	(31.01)	35.12	(31.33)	56.31*	(28.55)
Industrydummies	Yes		Yes		Yes	
Year dummies	Yes		Yes		Yes	
Country dummies	Yes		Yes		Yes	
No. ofobservations	13,185		13,185		13,185	
Model fit						
Wald χ2-statistic[a]	956.72 (53)		931.42 (55)		950.10 (55)	
Arellano–Bond test (Π1)[b]	−10.38 [0.0]		−10.01 [0.00]		−9.58 [0.00]	
Arellano–Bond test (Π2)[b]	1.56 [0.12]		1.61 [0.11]		1.28 [0.20]	
Hansen J-statistic[b]	76.54 [0.31]		54.76 [0.56]		58.05 [0.20]	

[a]Degrees of freedom in parentheses.
[b]z-values are reported with significance levels in brackets.
***$p < 0.001$; **$p < 0.01$; *$p < 0.05$; †$p < 0.1$, system GMM estimation.

positive effects of having prestigious directors on the board. As Model 3 shows, the interaction term is indeed negative and significant ($p < 0.05$), supporting Hypothesis 3. Due to the high correlation of both interaction terms (see Table III), we decided follow the approach of used in Atanassov and Kim (2009) and estimated regressions with interaction effects separately. The significant interaction term is plotted in Figure 1.
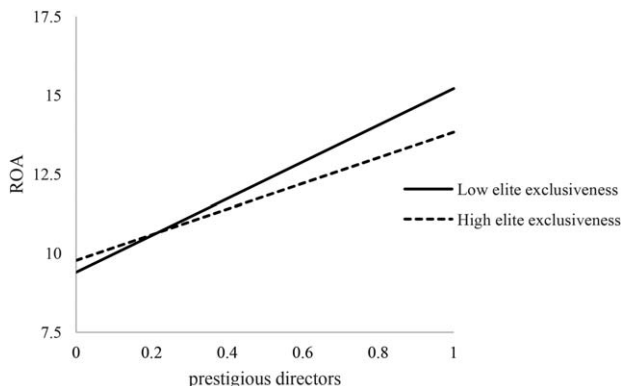
Figure 1. Interaction effects for elite exclusiveness
Notes: Low and high levels for the moderator imply values of one standard deviation below and above the mean.

Following Shaver (2008), who claims that 'concluding that an effect is non-zero is different from concluding that an effect is meaningful' (Shaver, 2008, p. 187), we also had a look at the economic significance of the performance effect of prestigious directors. Following previous research (Masulis et al., 2007), we calculated the change in the dependent variable when the independent variable changes by one standard deviation (SD). As model 3 indicates, the coefficient of prestigious directors is 6.03. Hence, a one SD change in prestigious directors results in a performance increase of 2.23.

Robustness Tests

To address the concern that the volatility of the exclusiveness moderator across time might have undesired effects on our results, we decided to additionally approximate elite exclusiveness by the time-invariant measure of social immobility. Hence, as a robustness test for the exclusiveness moderator, we used the social immobility measure of the OECD described earlier. We find support ($p < 0.05$) for the hypothesized direction of Hypothesis 3 in Model 4 (Table V). Another possible concern is the validity of the specification of our prestige and elite measures. To check for the sensitivity of our results regarding the chosen thresholds, and to check for the possible overestimation of the significance due to artifacts in the data, we recalculated our model with changes in the variable specification. As described above, prestigious directors are identified using the top tercile of the ranked list of the directors in a country. Model 5 (Table V) represents the results using the top quartile. Models 6 and 7 (Table VI) show the estimations for the exclusiveness measure with a threshold of 35 firms and 45 firms. Estimations for the cohesiveness measure with the same respective thresholds are not displayed in the study. The interaction effect of elite cohesion remains insignificant with these changes thresholds.

In further tests, we challenged the robustness of our results with respect to differences between one-tier and two-tier board systems (for details about potential differences between these board systems see e.g., Heyden et al., 2015). Controlling for the differences in country-level board systems does not change our results.

Table V.   Regression results – robustness

Dependent variable	Model 4 ROA		Model 5 ROA	
	Coeff.	S.E.	Coeff.	S.E.
% prestigious directors	4.37**	(1.62)		
Social upward immobility	−126.51	(161.90)		
% prestigious directors *social upward immobility	−31.30†	(17.77)		
% prestigious directors (quartile cut off)			6.15**	(2.26)
Board characteristics	Yes		Yes	
Ownership characteristics	Yes		Yes	
Firm characteristics	Yes		Yes	
Industrydummies	Yes		Yes	
Year dummies	Yes		Yes	
Country dummies	Yes		Yes	
No. of observations	13,185		13,185	
Model fit				
Wald χ2-statistic[a]	1111.41 (50)		621.70 (53)	
Arellano–Bond test (Π1)[b]	−10.14 [0.0]		−9.40 [0.00]	
Arellano–Bond test (Π2)[b]	1.52 [0.13]		1.01 [0.31]	
Hansen J-statistic[b]	60.51 [0.49]		38.96 [0.87]	

[a]Degrees of freedom in parentheses.
[b]z-values are reported with significance levels in brackets.
***$p < 0.001$; **$p < 0.01$; *$p < 0.05$; †$p < 0.1$, system GMM estimation.

To account for potential issues of endogeneity and reverse causality, we first replicated our results employing country-level elite adjusted measures of board prestige (prestigious directors adjusted is the residual of an OLS regression of prestigious directors explained by elite cohesion and elite exclusiveness). We were able to replicate our results using this adjusted prestige measure. Second, we calculated reverse logit regressions explaining the growth of boards and the substitution of less prestigious directors with more prestigious directors to contend that firms with high performance do not attract more and more prestigious directors. To save space, the robustness results are not presented in the paper.

DISCUSSION AND CONCLUSION

This study sheds new light on the performance effects of prestigious directors. By introducing the institutional level factors to research on the effects of prestigious directors, our study contributes to further disentangling the cost and benefits of prestigious directors. We have shown that prestigious directors on boards may bring both benefits and costs to firms. While our result indicates that prestigious directors generally contribute to firm performance, costs of such directors emerge under some institutional conditions. These costs, due to the elite-favouring behaviour of prestigious directors, likely occur especially in countries with high levels of elite efficacy. To comprehensively depict elite

Table VI. Regression results—robustness

Dependent variable	Model 6 ROA		Model 7 ROA	
	Coeff.	S.E.	Coeff.	S.E.
% prestigious directors	5.81**	(1.78)	5.89**	(1.86)
Elite excl. (35 firms)	−0.09			
% prestigious directors * elite excl. (35 firms)	−2.56**	(0.41)		
Elite excl. (45 firms)		(0.85)	0.24	(0.39)
% prestigious directors * elite excl. (45 firms)			−3.11**	(1.02)
Board characteristics	Yes		Yes	
Ownership characteristics	Yes		Yes	
Firm characteristics	Yes		Yes	
Industrydummies	Yes		Yes	
Year dummies	Yes		Yes	
Country dummies	Yes		Yes	
No. ofobservations	13,185		13,185	
Model fit				
Wald $\chi2$-statistic[a]	979.61 (55)		942.56 (55)	
Arellano–Bond test $(\Pi1)$[b]	−12.88 [0.0]		−9.51 [0.0]	
Arellano–Bond test $(\Pi2)$[b]	1.07 [0.28]		1.29 [0.20]	
Hansen J-statistic[b]	56.91 [0.18]		57.05 [0.23]	

[a]Degrees of freedom in parentheses.
[b]z-values are reported with significance levels in brackets.
***$p < 0.001$; **$p < 0.01$; *$p < 0.05$; †$p < 0.1$, system GMM estimation.

efficacy, we developed the institutional variables of elite cohesion and elite exclusiveness as important contingencies that affect the performance implications of prestigious directors. We have shown empirically that both dimensions of elite efficacy reduce the positive performance effects of prestigious directors, however, only the effect of elite exclusiveness is significant. By doing so, our study makes several contributions and suggests a future research avenue, as we discuss below.

Research on Elites

Our study offers implications for research on elites and their role in the corporate world. We have shown that the societal effects of elite-favouring behaviour can affect economic outcomes at the firm level. Hence, we combine the macro-level perspective of societal elite characteristics with the micro-level effects of corporate actors such as board members on firm level outcomes. This integration of the micro and macro perspectives on elites adds to research on the role of elites in corporate governance research (Davis et al., 2003; Jensen and Zajac, 2004). While previous research pointed out the relevance of characteristics of elites on individual (Jensen and Zajac, 2004) and company level behaviour (Hage and Dewar, 1973), our study demonstrates the importance of also considering elite structures at the country or institutional level. The institutional characteristics of elites thus deserve closer attention in the management research. With elite

cohesion and elite exclusiveness, we introduce a framework that describes elite efficacy at the institutional level. This framework can be applied in a broad range of corporate governance studies. Future research might, for instance, seek to investigate the effects of elites on the likelihood of CEO dismissals or managerial compensation in different institutional contexts with unique elite structures.

Prestigious Directors

Mixed research evidence exists concerning potential effects of prestigious directors. Whereas some studies have found positive effects of prestigious directors (Certo et al., 2001; Pollock et al., 2010), recent research has highlighted the costs of prestigious directors (Acharya and Pollock, 2013). We built on these studies and attempted to identify conditions under which costs of prestige may be amplified or when costs outweigh the benefits of the rich capital of prestigious directors and of the positive signalling effect, thereby damaging firm performance. These thoughts are in line with the stream of literature that observed that social ties bring directors to bargain executive compensation contracts less strictly (Hwang and Kim, 2009) and to be less likely to dismiss low performing CEOs (Nguyen, 2012). Our study adds to this line of research, as the negative effect of the elite moderators generates a clearer picture of the underlying effects of the potential costs of prestigious directors. The negative effects of our institutional moderators provide empirical support for the existence of costs of prestigious directors.

With elite-favouring behaviour, we also model a potential cost dimension of prestigious directors in more detail. Our study demonstrates that researchers recommending the appointment of prestigious directors for the reasons of positive signalling (e.g., Certo et al., 2001) or rich director capital could extend their models by also considering potential cost that can occur due to elite-favouring behaviour. Our results may not only hold for the board context but also provide interesting insights for the effects of prestige and status in general. For instance, researchers that primarily focus on the prestige of other corporate actors such as TMT members (e.g., D'Aveni and Kesner, 1993; Lester et al., 2006) might want to apply our results to their context to challenge the idea of exclusively positive effects of prestigious managers. Their high status might lead prestigious managers to be easily infected by managerial hubris, which can raise costs for the respective company. From a more general perspective, our study follows the call for more research not only considering benefits of prestige-based status but also taking potential downsides into account (Chen et al., 2012).

Research on Comparative Institutions

Our results also demonstrate the importance of considering the institutional environment when investigating the effects of prestigious directors. Specifically, our study adds to the literature that emphasizes the value of multi-country studies for gaining insights on the effects of corporate governance characteristics (e.g., Aguilera et al., 2008; Boyd et al., 2011; Filatotchev et al., 2013; Hüttenbrink et al., 2014; Oehmichen et al., 2017b). While we acknowledge that governance systems may vary across national contexts based on different legislation, cultural traditions, and stakeholder considerations (Aguilera and Jackson, 2003), we aim to contribute to the literature by going beyond the

usual classifications of formal and informal institutions that describe a country's institutional environment. This study shows that specific institutional dimensions can be (and should be) selected and developed for the specific research questions (i.e., upsides and downsides of prestigious directors in this study). Since we were interested in the potential benefits and costs of elite-favouring behaviour, we constructed a framework of the elite that was based on institutional factors. With these specific variables depicting country-level elite structures, we add to research on the country-level effects of social capital.

A study by Burt and his colleagues (2000) indicates that country-level differences with respect to social capital effects exist, but their two-country research design does not allow researchers to specify the country-level effects and distinguish them from other formal and informal institutional characteristics. Extending this two-country approach to a multi-country study allows us to distinguish country-level effects more specifically. Future research might want to follow our strategy to develop case-specific institutional dimensions. For instance, research on the potential of stakeholder-favouring behaviour might need to develop specific institutional frameworks describing the institutional stakeholder orientation based on formal and informal institutional factors. By modelling institutional environments in this manner, researchers can clearly extend the institutional research that has primarily focused on established classifications of regulative, normative, and cognitive institutions.

Limitations and Future Research

As in other studies, our research is not without limitations. First, our study does not examine the underlying board mechanisms that actually contribute to or damage firm performance. Future studies might want to add to our research by questioning how the institutional elite efficacy influences effects of prestigious boards on outcomes of specific board tasks such as monitoring the CEO (Kroll et al., 2008) or providing strategic counsel (Oehmichen et al., 2017b; Pugliese et al., 2009), which in turn impacts firm performance. Additionally, these studies may want to further challenge behavioural consequences of director prestige. Potential questions might be whether director prestige increases the number of lawsuits against elitist behaviour and which specific deviations from the norm we can observe in firms with prestigious directors.

Second, we looked at elites at the country level. With this simplification, we indirectly presumed one elite group per country and that the institutional variables that depict the elite structures do not change between different regions within each country but are rather homogeneous across all regions of a country. This is a simplification from which most studies concerning institutional or cultural differences suffer (Kirkman et al., 2006), although researchers have indicated the importance of within-country differences (McSweeney, 2002). Therefore, future research could consider within-country differences in a country's elite structures, for example, by opposing East- and West-Coast elites in the USA or specific elites of metropolitan areas, such as the region around Frankfurt in Germany or Paris in France. We would expect to see an increase in the effect of elite moderators due to the higher cohesiveness of the networks in these regions.

Third, although we theorized the effects of social interaction between the members of the elite, we were not able to measure these interactions. Thus, future research might

further open up the black box of social interaction and friendship ties between the members of the countries' elites, although previous research indicates that to truly measure this interaction, survey data is required (Westphal and Stern, 2006, 2007; Westphal et al., 2006). For the multi-country focus that our research requires, this would be a challenging endeavour. Furthermore, the multi-country setting of our study did not allow us the use of in-depth prestige measures and the investigation of in-depth group behaviour effects in boards with prestigious directors. Future single-country studies, however, could address this point. In-depth studies could examine whether different sources of prestige (e.g., corporate vs. educational) have different effects on director performance, if these sources of prestige rather substitute or complement each other, and if these sources of prestige result in different group dynamics, such as decreasing group effectiveness as a result of too many prestigious directors (Groysberg et al., 2011), informal hierarchies in the group of directors (He and Huang, 2011), differences in board members participation in boardroom discussions (Pugliese et al., 2015) and group polarization (Zhu, 2013).

Lastly, our study focused on Europe and the USA – both Western industrial market countries. Hence, we ignored potential institutional effects prevalent in Asian countries or in emerging markets. These regions might be fruitful future research extensions because Asian countries differ from Western countries in terms of several institutional and cultural dimensions. Emerging markets would additionally allow for modelling the effects of institutional change since most of these countries are in a period of transition. This transition might also affect the formation and structure of the countries' elites. Hence, we hope that our study encourages future research reconsider our elite measures in different institutional settings and thereby also help to extend reliability of our conceptualization of country-level elites.

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NOTES

[1] Some studies have used the term status instead of prestige, and have examined the effects of high status affiliation, instead of referring to prestigious affiliations (Benjamin and Podolny, 1999). While we included these studies in our theoretical framework, we followed the approach of Acharya and Pollock (2013) which considers prestige and status as synonyms, and used the term 'prestige'. To assure the comparability of prestige between the different countries in our sample, we concentrated on directorates as a source of prestige.

[2] Conceptually, the exclusion of executive board members enhances the comparability of the countries in our sample (in Europe, one- and two-tier board systems are prevalent (Heyden et al., 2015; Thomsen and Conyon, 2012)) and the focus on non-executives more strongly connects our measure to our theoretical reasoning. We suggest that prestigious directors may potentially neglect their monitoring duties. These monitoring duties are primarily the task of non-executive board members.

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