World Academy of Science, Engineering and Technology
International Journal of Economics and Management Engineering
Vol:9, No:05, 2015

# What Do Board Members Learn from Their External Connectedness? The Case of Firm Diversification

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**Abstract :** Using a dataset consisting of 7,120 firm-year observations from the Taiwan stock market over the 2007-2011 sample period, we find a significantly negative relationship between board external connectedness and firm diversification. We propose a learningeffect hypothesis indicating that an externally connected board member's experiences in other companies directly affect his recommendations regarding the underlying firm's diversification. The partial correlation between diversification and the performance of firms with externally connected board members is used as a proxy for the learning effect. The empirical results show that the learning effect is asymmetrically embedded in firm diversification, with negative experiences having a greater effect on firm diversification than positive experiences. Externally connected board members are associated with reduced diversification in one firm after they learn that diversification is detrimental to value in other companies. Moreover, the diversification of a firm due to board external connectedness is moderated by the controlling owner's interest alignment and entrenchment.

**Keywords :** board, external, connectedness, diversification
**Conference Title :** ICEF 2015 : International Conference on Economics and Finance
**Conference Location :** Berlin, Germany
**Conference Dates :** May 21-22, 2015