

**IMPACT OF POLITICAL CONNECTIONS ON BANK PERFORMANCE:
THE MODERATING EFFECT OF BOARD GENDER DIVERSITY**

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ABSTRACT

This study aims to investigate the role of gender diversity of board members in order to explain the influence of political connections of board members on the performance of the banks based in Pakistan. The paper analyses the data introduced as a panel of 21 banks for the period described as 2015-2019 using panel regression along with the moderation analysis as methodology. Results suggest that banking performance is positively influenced by political connections. This means that personal interests of members having political connections do not overlap with the interests and goals as well as prosperity of the institution. Board gender diversity does not exhibit any sort of effect to mitigate or to accentuate the impact of political connections on bank performance. The results of the study revealed that politically connected board members can help to maximize bank's profitability. Women on board may increase firm's risk due to their inclusive behavior of possessing more risk aversion than men which could lead to lower expected returns. The research may not precisely predict the suitability of board members assessment. The effect of board gender diversity has not been studied widely and this research will help to lay the basis for conducting future research in this particular area.

Research Limitations: The impact of the board's appropriateness evaluation may not yet be completely reflected in the time period investigated.

Practical Implications: The paper plays a great role in the contributing in literature on political connections and board gender diversity taken as determinants to evaluate banking performance, the study also primarily focuses on the advantages and disadvantages that could fall into place due to the quota systems in Pakistan.

KEYWORDS

Political Connections, Board Gender Diversity, Bank Size, Leverage, Capitalization, Managerial Efficiency, Non-Operational efficiency.

1. INTRODUCTION

The proper functioning of economy depends upon the sound, secure and healthy financial system of a country. The financial sector of a country plays a critical role in its economic development (Khan et al., 2021). However Pakistan faces severe challenges because of its unstable economy and political conditions. Since Pakistan has come into

existence its economy has consummated over 25 different governments. Thus Pakistani Financial sector has experienced a lot of suffering because of changing fiscal policies and due to high political hindrance by government (Haris et al., 2019).

The economic growth of a country and stability of banks require sustainable profitability (Garcia-Herrero et al., 2009). The financial sector is considered as one of the indispensable constituent of the monetary industry which is assumed to be the support of the economic growth of a country (Butt et al., 2018). The economic growth is directly proportional to the sustainability of profit of banks and other financial mediators (Haris et al., 2019). So the sustainability of banks all around the globe is of vital importance as it allows banks to continue their role in the economic growth and development of the country. For a functioning economy there is always a need of stable and sound financial system. However banking sector faces a lot of troubles and daunting regimes mainly because of the instability of the political system. This study contributes to the literature in many ways. The matter of political connections of BOD has recently gained a lot of attention. The performance of the banks is highly influenced by the political interference. Another study predicts that the performance of banks is prejudiced majorly due to the higher preferential bank loans (Khawaja & Mian, 2005). In addition to this Yao et al. (2018) revealed that banks display lower profitability at times of government changeovers and suggested that the lower return is due to the political connections. Political connections may be a double-edged sword to a firm (Pang et al., 2021).

The composition of board of directors (BOD) has been conferred on receiving a lot of attention from shareholders and investors (Tanka, 2019; Wang et al., 2018). This particular matter has been in the news following the financial scandals that have been witnessed in recent years (2008 financial crisis and WorldCom bankruptcy) which has driven the urge of improving the potency and efficacy boards (Nyamongo and Temesgan, 2013; Reguera-Alvardo et al., 2017). The board of directors possesses different qualities, knowledge and characteristics that as a whole contribute towards a success or failure of the company (Abid & Ahmad, 2015; Walt & Ingle, 2003). One of these characteristics political connections of board of directors is considered to be very crucial (Abid & Ahmed, 2014; Chen et al., 2018; Lin et al., 2015; Woong & Hooy 2018). Secondly adopting strategies and policies that include people from different traditions and cultures in an organization in order to maintain an comprehensive culture (Farooqi et al., 2017; Herring, 2009) with an accentuation on gender diversity (Adsuei et al., 2017; Garcia-Meca et al., 2018; Owen & Temesvary, 2018; Rodriguez-Ruiz et al., 2016). Gender diversity is a major favorable predictor of bank performance in Nigeria, according to a research, but board independence is a significant negative predictor (Okoyeuzu et al., 2021).

Prior studies are evident that politically connectedness can affect a firm's performance both positively or negatively. Political connections can provide a company with an increase in its sales and an easy approach to the credit markets with relatively decreased interest rate of return (Su & Fung, 2013). This can lead to the increase in the performance level of the company along with the reduction in the operational risk by providing an informal protection mechanism (Song et al., 2016). Firms can also utilize their political connectedness to over interest because they have an easy access to long term financing (Ling et al., 2016). Board of directors with political connections are also seen taking advantages of these connections for their personal interest which can be detrimental for the

collective good of the company (Saeed et al., 2016) and for the wealth of stakeholders (Bebchuk & Fried, 2004). It is very important to sustain profitability for banks in or to maintain its stability (Garcia-Herrero., 2009). Sinha & Sharma (2016) suggested that the development of a country is also dependent upon the profitability of banking sector. Financial sector is said to be the most important factor for the development of the country economically (Haris et al., 2019). Therefore it is really important for Pakistani banking sector to thrive for profitability as it has the most important role in the stability of the country.

Political connections can also affect corporate governance of a firm. Political connections can lead towards the agency problems because politically connected leaders are only concerned about their personal interests and are not concerned about the maximization of shareholders wealth. However politically connected firms are more exposed towards the risk because these firms have to provide more loans on a relatively lower cost which in return increases the risk of the firm. It can be said that political connections of leaders have different advantages and disadvantages when it comes to financial and non-financial firms. The studies conducted by Chen et al. (2018) revealed that banks having politically connected leaders tend to have lower performance when compared to banks having board of directors with no political connections. Moreover firms having politically connected leaders depict a very high ratio of defaults because such leaders take advantages of their political power and provide loans based upon their political connection resulting in defaults causing lower profitability. This is the reason that banks in Pakistan depict a very poor performance in terms profitability in election years. Hung et al. (2017) revealed that banking performance is suffered due to politically connected leaders. His study investigated that Pakistani banking sector suffers negative impacts of politically connected leaders.

According to the agency theory when comparing men and women, women are more likely to screen management performance more diligently (Abid et al., 2014). Women are more ethically concerned risk averse and conservative (Ku Ismail & Abdul Manaf, 2016; Palvia et al., 2019). So women in board of supervisory directors can limit unethical practices hence increasing the cost-effectiveness of banks and magnifying the returns on average assets. A market that financially stable can allow the possessions obtained from banking sector to be utilized at their best capacity that enables the economic development (Mayur & Saravanan, 2017; Pathan & Faff, 2013). The results of board diversification and performance of a firm are still a bit inconclusive. The main reason for this inconclusiveness is the misrepresentation of women on the decision making boards. Lakhil (2015) explained that many countries are working on forming legislations and female quotas in order to appoint more women on the supervision boards to promote board gender diversity in their firms. Because according to most of the studies gender diverse firms are tend to produce more profits and get more gains when compared to firms that are not gender diverse (Carter & Dsouza, 2010). Teijan (2011) postulates the female quotas are the only way to create a gender balance in the corporates. Another study revealed that creating laws and legislation to appoint women on board will result in the balanced representation of women present on the board. The increased number of women on board will lead to proper monitoring which can enhance the performance and profitability of the firm (Bebchuk & Fried, 2006).

However some studies also reveal that creating such quotas can lead to the hiring of women with fewer competencies which can lead towards the lower performance of the bank.

The literature is very vast when dealing with relationship among gender diversification and performance of the firm. However very scarce literature is to be found that explains any results regarding the effect of diversification of gender on minimizing or maximizing the political impact upon firm performance. The literature regarding diversification of gender is being studied widely in recent years but no conclusive results have been yet found. A study conducted by Owen and Temesvary (2018) reported a nonlinear relationship among banking performance and board gender diversity. They suggested that as the women on board increases it increase the board interactions resulting in the non-profitability of banks. This research will serve as the basis for the further future directions for many researchers working under these variables. Most of the studies done in the firms that are not involved in financial sector suggested that political connectedness can help these firms to gain more loans at a lower interest rate. Firms appoint leaders with political connections because they want political grants and benefits from them (Jackowicz et al., 2014). This politically connected board of directors uses the capital of the bank in order to fund their electoral campaigns. Pakistan is a politically influenced economy and most of the banks in Pakistan are keen to form links with people having political connections. They use these links later to gain monetary as well as non-monetary benefits. Non-monetary benefits include reduction of taxes, relaxation during government audits, tax subsidies and much more (Cheema et al., 2006).

2. LITERATURE REVIEW AND HYPOTHESIS DEVELOPMENT

Politically Connected Directors: The governments and banks are closely linked to each other with a continuous intrusion of politics and politicians on all sorts of business activities (Hillman, 2005). Our scientific community corresponds to these links as political connections which aims to achieve the gain of power (Wong & Hooy, 2018). As observed through the prior studies the element tends to have a political connection whether male or female with a political background that could be an official of government, advisor or a politician in ministry (Caretta et al., 2012; Garcia-Meca, 2015; Hung et al., 2017). An economy that is politically infiltrated, banks provide sufficient loans at a relatively lower interest rate at more advantageous terms to the firms which have political connections. The ultimate advantage of such loans is essential for politicians because it supports politician's electoral campaign ultimately suppressing the ability of management to achieve sustainable business growth. The board of directors who are politically connected impact the board decisions that influence bank performance (Liang et al., 2013). The political connections and its impact on non-financial firms were studied extensively by Boubakri et al. (2008). The political connectedness and its impact on financial institutes were studied by Berger et al. (2009).

The presence of political connectivity can also be justified through Resource Dependence Theory. According to which, companies are in a constant need of acquiring and exchanging resources which leads to the dependence among the companies and governments or any other external units (Decaba et al., 2012). Dependence causes uncertainty and risks that can be minimized through creating political connectivity and provides the company with a strong resource base that ultimately improves the firm's value

(Wong & Hooy, 2018). Moreover political links can also lead towards agency theory. Jensen and Meckling. (1976) proposed this theory according to which the separation between the managers and shareholders creates agency problems which provides incentives to board members who have political connections that are used by them to magnify their personal interests (Bebchuk & Fried, 2004) which is indirectly detrimental for the interest of shareholders. The effects of political connectedness is being widely studied with the range of standpoints one of them being impact on performance on financial institutes (Wong & Hooy, 2018). Two of the other perspectives were also considered while observing the effects of political connects that are fiscal policies and job creation (Lin et al., 2015; Mennozi et al., 2012). Nevertheless the impact of described impact on activities of business displays both positive as well as negative effects.

It can be observed that companies with political connections can obtain bank loans and investment projects (Wang et al., 2018) more easily in contrast to the firms having no political connectivity at all. In addition to this the firms having more connections with politicians tend to face lower taxes more green grants and have a better chance of entering into industries with high barriers (Chen et al., 2014). Studies have shown that political connections positively influence the employment and provides for higher liberation probability for the companies when they are stuck in certain hardships in the economy leading towards lower capital cost and risk reduction (Boubakri et al., 2012). However literature also suggests that there are political connectivity can also induce negative effects on the activity of the business. The companies having strong political connectivity tend to be high interest and possess low level of productivity along with high debt ratio (Domadenik et al., 2016; Faccio, 2010).

As far as the banking sector is concerned the literature is still very limited. A research conducted in banks in the context of China according to which the banks with political connections can take benefit from the process of providing loans to companies having political connections which are recognized as assets having high quality because in case of financial difficulties they are more likely to be bailed out (Hung et al., 2017). On contrary to this Chen et al. (2018) carried out an analysis on the sample of 41 banks from different countries which led the results that politically connected banks lead to decreased performance because of the lessening provided in loan loss risk analysis. The study also explains that political connections lead to poor performance since politically connected board members are more curious about their personal interest and by approving non profitable projects (Garcia-Meca & Garcia, 2015).

A firm is described as a having political connectivity if the board members as well as its leaders are primarily involved in activities have , have ties with political government leaders and have a strong political career in past (Gilbert, 2011). Most of the studies are concluded by the researchers to verify the advantages of political connectivity for firm's profitability. Some of these major advantages include the companies that are politically connected tend to get credit access more easily when compared to the companies that are not politically connected (Yeh et al., 2013). Some other researches being conducted revealed that politically connected firms get more leverage against a very minimum interest while producing absolutely not guarantees (Chen et al., 2011; Faccio, 2006). Some of the other researches reveal that firms having political connections tend to get government grants contracts (Batta et al., 2014). The prior studies also identify that political

connectivity can help to decreased amount of taxes for a firm (Wu et al., 2012). Correia (2014) explained that firms that are politically connected are very less likely to be tracked by security agencies because of the influence of their political connections. However some of the researches also revealed that political connections of firms leads towards a negative impact on the firm's profitability (Liu et al., 2013). Some other studies revealed that political connections of firm's leaders tend to make a bad impression about firm's value (Fan et al., 2007)

Hillman et al. (2009) revealed a firm is usually system that depends on its resources for its growth and survival. This theory emphasizes on the importance of political links of board of directors as board of directors are the ones who serve as a provider of resources for the company that are missing in its internal environment. In the external environment political connections are considered as a major force. Political connectedness is considered as the strong basis for resources obtained externally (Hillman et al., 2009). Pfeffer (1978) suggested that as far as resource dependency is concerned firms are always in an urge of bonding links with personalities having political connectivity to lessen its dependency on resources which are in control of the external figures. According to this theory political connections serve as a basis to manage uncertainties that are caused due to the external environment. The political connections are a result of government incorporations of board of directors or their amalgamation in political parties as suppliers of resources when the company is in the need of external or internal resources. The influence of political ties on loan interest rates suggests that the supply side is driving credit smoothing behavior (Bian et al., 2021).

Most of the studies predict positive impact of political connectedness and performance of the firm (Bona-Sanchez et al., 2014; Jockowicz et al., 2014). It is observed that political connections can provide an accession of resources by means of loans, green grants through governments and government contracts which ultimately increases company's performance and its value. Some other researches revealed that political connections give rights rise problems regarding agency theory (Ding et al., 2015) Another study performed by Su et al (2014) shows that board members having political connections can exploit the rights of minority of shareholders ignoring the maximization of shareholders wealth. Political connectivity can lead towards the hiring of people with political connections which can cause a problem for company's value (Cao et al., 2011). It is observed that political connected board of directors tend to make decisions that are not generally in the favor of the shareholders and lead towards damage of the company's goodwill and value of the firm can be compromised.

Jackowicz et al. (2014) revealed his results by using a sample polish firms. According to his findings political connectedness tends to influence the firm's returns negatively. Jaffar and Abdul-Sukor (2016) suggested his results in one of his research on Malaysian firms. According to his results political connectivity influences the performance of a firm negatively. Findings of his research are far most suggesting that political connections could actually demolish a company's performance. In a politicized form of economy banks usually provide loans at a relatively low rate and more promising terms and conditions to the companies which have strong political relations with political parties. The directors having political connections tend to influence the decision of the board at the cost of bank's goals and such type of influence causes an adverse effect on bank's performance (Liang et

al.,2013).Some of the other studies revealed that lending decisions of bank are effected due to political connections of its leader which influence the performance and profitability of the bank negatively (Fam et al., 2007).Politically connected board of directors tend to provide loans at a very minimum interest rate to the political parties to run their electoral campaigns and such type of loans sometimes hinders the management of a bank to achieve its yearly goals and objective.

Micro et al. (2007) suggested that banks lend money at a lower interest rate during the election season which later lies as a basis of non-profitability of banks during the election year. The theory of network explains that the monetary funds and resources are easily granted to the firms having political connections because of their strong network with government. Many others studies suggested that bank's profitability is seen to be lower in elections years due to the political connections of bank's leaders (Cole, 2009).Many studies support these results that political interference are detrimental for bank's profitability (Yao et al., 2018). Moreover another study revealed that bank's performance is seemed to be very lower in terms of its profitability during election year (Haris et al., 2019).Loan loss provisions are represented in the liabilities side in a balance sheet however it is recorded as an expense in the income statement. Loan loss provisions represent overdue credit which helps in the analysis of credit risk. Nowadays banks are exposed to failure because of the enormous amount of money they have provided to their customers in the form of loans. In order to overcome such risks loan loss provisions are kept by the banks to overcome overdue credit risk. Hence this proxy is used to measure the profitability of the banks and other financial institutes. Tahir et al. (2014) investigated the effects of loan loss provisions on the profitability of banks in Pakistan. He used Return on Assets and Return on Equity as the basis of profitability proxies. His study revealed that loan loss provisions have a negative effect on the profitability of the bank. Higher the loan loss provisions lower the profitability and stability of the bank. Mustafa et al. (2012) also examined the banks of Pakistan over the period of 2001-2009. However their study revealed the same results as Tahir et al. (2014). These results were in line with the fact that increases in loan loss provisions causes a decrease in the profitability and stability of the banks.

In the view of above described findings, the following hypothesis is formulated.

H1: Political Connections of Board of Directors has a significant effect on the bank performance

Gender Diversity of Board of Directors: Many researches have been done to investigate the effect of diversification of board on the performance of firm. However the literature regarding banking performance is still very rare to be found. There exists recognizable evidence that gender diversity has an effect on performance of the firm (Simkins & Simpson, 2010). The impact of gender diversification and performance of the firm is of great concern for the composition of board (Lukerath-Rover, 2013; Soobaroyen & Hanuman, 2012). However the research done regarding gender diversification and performance of the firm has not yet provided any conclusive results. Simkins and Simpson (2010) suggests that there board gender diversity impacts the performance of the firm positively. Minguez-Vera (2008) reported similar results. Rose (2007) revealed that there gender diversification and performance of the firm are not significantly impacting each other. Sinclair-Desgagne (2008) conducted a research in UK and concluded that performance of the firm is neither increased nor decreased due to the presence of women

on the board. Later comparable results were reported by Trojanowski and Atkins (2010). However Ahern and Dittmar (2012) suggested that there exist a gender diversification of board influences performance of the firm negatively when he conducted a research on Norway as the Norwegian government imposed forty percent imposition of women quota on supervisory boards. Most of the countries have made women quotas a compulsion in their supervisory boards. However less competent women are appointed through these quotas resulting in an indirect impact of gender diversification on performance of the firm. Gender diversity is also linked to bank performance as measured by ROA and Tobin's Q, as well as dividend payment ratios, implying that female directors are better monitors than male directors (Cardillo et al., 2021).

As far as gender diversity is concerned. In most studies it can be easily observed that in major companies women are underrepresented as board of directors around the globe (Lee-Kuen, Sok-Gee & Zainudin, 2017). Many countries around the world especially European Union has set a quota for women in board of directors since they believe that diversity predicts really positive effects on business as already explained by behavioral finance. Croson & Gneezy (2009) suggested that behavioral finance suggests that male and female display behavioral differences. For instance women tend to be more risk averse. They have flexible preferences and are more competitive. Ku Ismail & Abdul Manaf (2016) suggested that women are more concerned in terms of ethics and good conduct. In terms of proposing strategies women are being less aggressive. They invest more in sustainability initiatives and are less directed towards investing in research and development projects (Apestequia et al., 2012). Galbreath (2018) concluded that women are more socially responsible so the companies they work in also possess more CSR. However studies predict that men are overconfident when making decisions (Hunag & Kisgen, 2013).

Literature regarding relationship between board gender diversity and performance of the firm shows mixed results. Since prior studies predict that board gender diversity promotes performance of the financial firms (Reguera-Al varado et al., 2017). However at the same time some studies suggests that there exists no significant relationship between performance of financial firms and board gender diversity (Carter et al., 2010). Literature is becoming quite relevant in terms of the study that focuses completely on banking sector (Pathan & Faff, 2013). Some more studies (De vita et al., 2018) reveals that when compared to the other industries banking sector seems to be more conservative to appoint women at positions where they can actually make decisions. Cultural norms, stereotyping are the major reason for it. However there is an evident concern in management to strive for being more composed in terms of balance of gender and suitability of candidate for the work. This study can be anticipated as a contribution to the literature. Since prior studies are very scarce on the stated topic.

The prescribed study investigates that how board gender diversity impact the effect of political connections on banking performance. According to agency theory and according to Krisch (2018) women are more diligent at screening management. So monitoring of women can produce reduced agency costs that are caused due to political connections impacting performance. Since women are more ethically concerned, risk averse and conservative so their presence in the board can eradicate unethical practices that cause a reduction in profitability of banks along with depletion of the quality of asset of banks (Palvia et al., 2014; Ku Ismail & Abdul Manaf, 2016). Moreover gender diversity enhances

the independence and advisory functions of board (Zhou et al., 2019). Francoer et al. (2008) suggested that higher the women on board higher is the chances of expected returns. Smith and Verner (2006) regulated a study based on 2500 Danish companies and concluded that there is a direct statistically significant relationship among diversification of board and performance of the firm. A study conducted upon 65 Spanish firms revealed that there firm performance is positively influenced by board gender diversity (Campbell & Minguez-Vera, 2008).

Platengo and Remery (2016) suggested that gender diversification and performance of the firm does not show any sort of significance among them. The impact of gender diversification on the performance of the firm is somewhat mixed and totally depends upon the research methodology being used. When using a voluntary approach there exists a direct significant relationship among diversification of gender on board and performance of the firm while when using enabling approach there exists a negative impact of diversity of gender and performance of the firm and in some cases no significance is found among the two variables (La Belle et al., 2015). So women on board should be assigned voluntarily and not on the basis of some prescribed quotas. Ahem and Ditmar (2012) are of the view that although many countries are passing legislations for female quotas in boards of the firms but female should be hired on the basis of competency in order to avoid damage towards the shareholder's wealth. Bohren and Storm (2010) have statistically reported that women on board have a negative effect on the performance of the banks. Adams and Ferreira (2009) has revealed that presence of women entities on board creates a negative impact on the performance of the banks because over monitoring can lead towards the counter productiveness that could be harmful for a firm's performance.

In the view of above described findings the following hypothesis is formulated

H2: Board Gender Diversity has a significant effect on bank performance.

Moderating Effect of Board Gender Diversity: This research has been started to verify the number of scientific views given on the impact of political connections as well as diversity of the board on the performance of the bank. This research has been driven to contribute towards the literature in this regard because there is a lack of prior studies that could explain any sort of relationship among these variables. A study conducted by Kirsch (2018) women is tending to be more conscientious when compared to men. Women tend to perform better monitoring of the management. The better screening performed by women can reduce agency costs that are produced due the political connections and thus impacts the performance of a firm. These findings are also in line with the agency theory (Palvia et al). 2014 revealed that women are more orthodox and risk averse. Women tend to be more ethically concerned (Abdul Manaf, 2016). So this presence of women on board can hinder the unethical conduct caused due to political connections that in return would increase performance of the bank and may enhance the profitability ratios of the bank. Zhou et al. (2019) concluded that the presence of women on board tends to increases the independence of the board. Hence women on board may hinder the political connections that come in the way of board independence resulting in the increased performance of banks. A recent study conducted by Jose et al. (2020) revealed that political connections impact the return of average (ROAA) assets and return on average equity negatively. Furthermore they suggested that political connections of bank leaders cause increases in the risk of the bank. Moreover according to another study board gender diversity increases

the negative impact of political connections on the performance of the bank (Catarina Proenca, Mario Augusto & Jose Murteira, 2020). This study is in line with the results produced by Campbell and Minguez-Vera (2008) that shows that increased negative impact of political connections on the performance of the bank is due to hiring of women based upon quotas. The women appointed on quotas are tending to be less competent (Ahern & Dittmar, 2012) that contributes towards lower performance of the bank. A research identified a relationship between gender diversity and bank performance as assessed by ROA and ROE, as well as a link between female board members and higher default risk as evaluated by Z-score (Othmani, 2021).

Some studies emphasize that the different and no significant effects on bank performance and diversification of board of directors (Colarbo & Huse, 2011). Erkut and Konard (2008) revealed that there should be at least three women appointed on the board in order to get an affiliation between impact of gender diversity and its effect on of corruption and unethical concerns of board members on firm performance. Joecks et al., (2013) investigated the board of 151 German stock exchange companies and predicted a negative relationship between firm performance and board gender diversity. Moreover he revealed that there must be three women appointed on the board for analyzing any sort of significance on predicted variables. Some other studies revealed that appointing at least three women to board of supervision could lead towards the better decision making by examining a sample of 99 Dutch companies (Lukerath-Rovers, 2013). This can lead towards the minimized negative effects of political connections on the firms by taking decisions that are in the favor of shareholders wealth. As with more women on board the viewpoints of among the board meetings increase which can lead to a better firm performance. Torchia et al. (2011) suggests same results regarding a study conducted upon 131 Norwegian companies during the year 2005-2006. According to him there should be at least three women appointed on a supervisory board for a firm to generate maximum profits and minimize risk. Females are said to be more responsible when appointed as directors because they serve as a linkage between the firm and its stake holders and serve a better resource for the firm (Shrophshire & Canella, 2007). Hence there should be at least three women among members of the board in order to get significant results when conducting any analysis.

In the view of above described findings the following hypothesis is formulated

H3: Board Gender Diversity moderates the effect of political connections on banking performance.

3. VARIABLES, SAMPLE AND MODEL

3.1 Sample Used in the Study

Sample is selected on the basis of proper representation of the variables under study that are Political Connections, board gender diversity, Bank size, capitalization, leverage, managerial efficiency and non-operational efficiency. To conduct this study the banking sector of Pakistan is taken. Foreign banks have been excluded leaving the local banks to be taken as a sample. This study does not focus on investment and micro finance banks as there is a major difference in their operations because these banks are not primarily involved in with lending and crediting of money. The focus of this study is commercial banks. The sample used in this comprises of 33 commercial banks out of which 29 are local

banks but the remaining four are foreign banks (yoo et al .2019). The focus of the study remains local banks. Out of the local banks, we have also excluded Muslim Commercial Bank, Islamic Bank as it was established in year 2015 and does not fulfill the requirement of data. Moreover the data for Dubai Islamic Bank Ltd, First Women Bank, MCB Islamic bank and Punjab Provincial Co-operative Bank Ltd was also not available therefore these banks are also excluded from the sample of the study. The banks like Zarai Taraqiati Bank and SME bank are not primarily involved in lending which is why these are excluded from the data sample. Final sample for the study remains 21 local banks that were operational during the time period 2014-2019, as these 96.5% of the share of asset in banking sector of Pakistan.

Data collection was conducted in two phases. During the first phase data was collected through the names of the board of directors of banks by using the financial and annual reports of banks. In second step the likelihood of political connectedness of these board members was verified by using biographies mentioned on bank's website, annual press releases, bank reports or by looking up to their LinkedIn profiles. Bank financial data was collected through bank's annual reports. We have hand collected the data on secondary basis through the statements of financial position, statements of profits and loss and through profiles of board of directors that were available on the bank's official websites as well as bank's financial reports. The data for measuring profitability along with data regarding bank-specific variables are also collected through bank annual reports.

Table 1
Banks Analyzed in Study

No#	Name of Banks
1	Albaraka Bank
2	Allied Bank
3	Askari Bank
4	Alfalah Bank
5	Al-Habib Bank
6	Bankislami Bank
7	Faysal Bank
8	Habib Bank
9	Standard Chartered
10	JS Bank
11	Muslim Commercial Bank
12	Meezan Bank
13	National Bank of Pakistan
14	Samba Bank
15	Silk Bank
16	Soneri Bank
17	Sindh Bank
18	Summit Bank
19	Bank of Khyber
20	United Bank
21	Habib Metropolitan Bank

Note. This table demonstrates the banks analyzed in this study.

3.2 Variables

3.2.1 Dependent Variables

According to the previous studies (Chen et al., 2018, Hung et al., 2017; Talavera et al., 2018) there are two proxy measures for measuring banking performance named as Return on Average Assets (ROAA) and Loan Loss Provision to Total Assets (LLPT). The variables ROAA are the measures for profitability and LLPT is a risk measure that helps to compute the assets of a bank. Return on average asset is a measure of bank's profitability however the increase in LLPT shows and increase in the overdue risk which is usually listed as non-performing loans in the portfolio of a bank.

3.2.2 Explanatory Variables

The explanatory variables which are taken as political connections of board members (POLBO) and women on board represented as (WBO). Political connection is measured through creating an indicator that is political connection on board (POLBO). It is measured by the percentage of member of board to the total board members (Caretta et al., 2012; Garcia-Meca and Garcia, 2015; Pathan and Faff, 2013). Political connections are taken as a measure of BOD that worked in the past as a politician, bureaucrat, advisor in ministry and former minister. Gender Diversity is measured through calculating the percentage of women on board to total board members as defined by Adusei et al. (2017), Garcia-Meca et al. (2018), Owen and Temesvary (2018) and Rodriguez- Reuz et al. (2016).

3.2.3 Control Variables

The control variables are the ones that are bank specific and can be change upon the changes made by the management of the bank. Following control variables are taken under consideration:

- Bank size is taken as the control variable (Caretta et al., 2012; Chen et al., 2018; Garcia et al., 2015; Hung et al., 2017; Talavera et al., 2018).
- Capital adequacy is considered as a control variable (Athanasoglou et al., 2008; Dietrich and Wenzelried, 2011; Garcia and Guerreiro, 2016; Talavera et al., 2018).
- Leverage is also taken as a control variable (Garcia-Meca and Garcia, 2015).
- Operational Efficiency of banks is also considered as a control variable (Garcia and Guerreiro, 2016; Hung et al., 2017).
- Non operational efficiency of banks is also taken as a control variable (Hung et al., 2017).

Operationalization of the variables is defined in Table 2 and Summary of descriptive statistics is being displayed in table 3. This should also be kept under consideration that the period under which these banks are being reviewed some banks also exhibited negative returns.

Table 2
Operationalization of the Variables

Variable	Codename	Formula	Reference
Dependent Variable:			
Banking Performance	ROAA	After tax profit/ Average Total Assets	Chen et al. (2018) ;Hung et al. (2017); Owen and Temesvary (2018) and Talavera et al. (2018)
	ROAA	After tax profit/ Average Total Equity	Chen et al. (2018) and Talavera et al. (2018)
	LLPT	Loan Loss Provisions/ Total Loans	Hung et al. (2017)
Independent Variables:			
Political Connections of Board members Board Gender Diversity	POLBO	Political Board Members/ Total Board	Caretta et al. (2012) and Cheng et al. (2018)
	WBO	Number of Women/ Total Board	Adusei et al. (2017); Garcia-Meca et al. (2018-2015); Owen and Temesvary (2018) Rodriguez-Ruiz et al. (2016)
Bank Specific Control Variables			
Bank Size	TA	Natural Algorithm of Total Assets	Caretta et al. (2012); Chen et al. (2018); Garcia et al. (2015); Hung et al.(2017); Talavera et al. (2018)
Bank Capitalization	ETA	Total Equity/ Total Assets	Athanasogloue et al. (2008); Dietrich and Wenzenried (2011); Garcia and Guerreiro (2016); Talavera et al. (2018)
Bank Leverage	LEV	Debt/ Total Equity	Garcia-Meca and Garcia (2015)
Bank Managerial Efficiency	CIR	Cost to Income Ratio: Total cost/Total Income	Garcia and Guerreiro (2016); Hung et al. (2017)
Bank Non-Operational Efficiency	NINC	Non-interest income/Total Income	Hung et al. (2017)

Note. This tables demonstrates the operationalization of variables in this study

3.3 Model

3.3.1 Regression Model

Following baseline regression models can be proposed for the developed hypothesis. In this study we have used multiple regression analysis in order to analyze the impact of multiple explanatory variables on the outcome variables. In this particular study we have analyzed the impact of explanatory variables and variable of interest represented as Return on Average Asset (ROAA) and Loan Loss Provisions to Total Equity (LLPT) respectively.

Table 3
Descriptive Statistics

Variable	Obs	Mean	Std.Dev	Min	Max
ROAA	105	.011095	.028814	-.0522511	.2320552
LLPT	105	.024371	.243756	-.284256	2.390224
POLBO	105	.137596	.135691	.0000000	.5714285
WBO	105	.042614	.057421	.0000000	.1666666
SIZE	105	26.9086	1.05997	22.96767	28.80261
ETA	105	.094455	.127951	.0240133	1.918922
LEV	105	.690033	1.93919	.1238518	14.56639
CIR	105	.771847	.477805	.2847930	4.148271
NINC	105	.339166	.271455	-.565129	1.734799

Note. This table demonstrates the descriptive statistics of the data

For concluding results regarding explaining the relationship between the explanatory variables following regression models are being used

$$Performance_{it} = \beta_0 + \beta_1 POLBO_{it} + \beta_2 WBO_{it} + \beta_3 SIZE_{it} + \beta_4 ETA_{it} + \beta_5 LEV_{it} + \beta_6 CIR_{it} + \beta_7 NINC_{it} + \varepsilon_i + \mu_{it}$$

Model 1

$$ROAA_{it} = \beta_0 + \beta_1 POLBO_{it} + \beta_2 WBO_{it} + \beta_3 SIZE_{it} + \beta_4 ETA_{it} + \beta_5 LEV_{it} + \beta_6 CIR_{it} + \beta_7 NINC_{it} + \varepsilon_i + \mu_{it}$$

Model 2

$$LLPT_{it} = \beta_0 + \beta_1 POLBO_{it} + \beta_2 WBO_{it} + \beta_3 SIZE_{it} + \beta_4 ETA_{it} + \beta_5 LEV_{it} + \beta_6 CIR_{it} + \beta_7 NINC_{it} + \varepsilon_i + \mu_{it}$$

i = Number of banks in the sample

t = Time period

β_0 = Intercept Coefficient

ε_i = random cross sectional effect

μ_{it} = error term

3.3.2 Moderation Model

To examine the moderating effects of gender diversification in explaining the influence of political connectedness of BOD on performance of the bank MRA that is Moderated Regression Analysis will be used. The board gender Diversity will be taken as an indicator WBO that represents the number of women present in BOD. The political connectivity of members of board will be represented by an indicator that is POLBO which is a representation of board of members having political background.

$$Performance_{it} = \beta_0 + \beta_1 POLBO_{it} + \beta_2 (POLBO * WBO)_{it} + \varepsilon_i + \mu_{it}$$

Model 1

$$ROAA_{it} = \beta_0 + \beta_1 POLBO_{it} + \beta_2 (POLBO * WBO)_{it} + \varepsilon_i + \mu_{it}$$

Model 2

$$LLPT_{it} = \beta_0 + \beta_1 POLBO_{it} + \beta_2 (POLBO * WBO)_{it} + \varepsilon_i + \mu_{it}$$

The interaction on this hypothesis is the multiplication between Political Connection and Board Gender Diversity. In order to validate this empirical specification hausman test has been conducted in order to decide between fixed or random methods.

4. RESULTS

4.1 Correlation Analysis

Table 4 represents the correlation analysis. The correlation Analysis exhibits that when political connections of the board of directors of a bank increase it simultaneously increases the profitability of the bank (increase in POLBO causes an increase in ROAA). Thus an increase in political connections causes a decrease in credit risk (LLPT). However the correlation between gender diversity (WBO) and performance indicators is somewhat different than that of political connections. The correlational analysis between the dependent and the independent variables can be seen below.

Table 4
Correlation Analysis

	ROAA	LLPT	POLBO	WBO	SIZE	ETA	LEV	CIR	NINC
ROAA	1								
LLPT	-0.68	1							
POLBO	.065	-.090	1						
WBO	-.028	.211	-.103	1					
SIZE	.186	-.82	.412	-.009	1				
ETA	.871	.011	-.027	.075	.002	1			
LEV	-.053	-.066	-.041	-.083	-.005	-.045	1		
CIR	-.339	.658	-.174	-.059	-.258	-.124	-.180	1	
NINC	.026	-.272	.110	-.231	.051	-.056	.014	.148	1

Note: This table demonstrates the correlation analysis between the dependent and independent variables.

4.2 Results for Base Models

The findings of present study (as shown in table 5 and 6) are that companies are in a constant need of acquiring and exchanging resources which leads to the dependence among the companies and governments or any other external units. Dependence causes uncertainty and risks that can be minimized through creating political connections and provides the company with a strong resource base that ultimately improves the firm's value. The results of this research comply with the findings of some other studies (Wong & Hooy, 2018, Decaba et al., 2012). It can be observed through the findings of present study that companies with political connections can obtain bank loans and investment projects more easily as compared to the firms having no political connectivity at all. In addition to this the firms having more political connectivity face lower taxes more green grants and have a better chance of entering into industries with high barriers leading towards the increase of profitability and performance. The results of present studies are also in line with the finding of similar studies (Chen et al., 2014, Wang et al., 2018). Banks with political connections can take benefit from the process of providing loans to companies having political connections which are recognized as assets having high quality because in case of

financial difficulties they are more likely to be bailed out. These results are also supported by Hung et al. (2012). However this study shows that board gender diversity has a significant negative impact on ROAA. Women are not comfortable with taking high risks but men do take high risks. Women do not take decisions having high risks due to which a bank can suffer in terms of returns. Moreover quotas assigned for appointing women on board can sometimes lead to a misrepresentation of women and impositions where non competent female members are hired which leads to a decrease in the amount of expected returns. These findings are also in line with some studies according to which gender diversity promotes financial performance (Garcia-Meca et al., 2015).

This study shows that board gender diversity has no significant impact on ROAA. The reason for no significant moderating effects is that the presence of women on boards of bank is very low. The Pakistani banking system is very stereotypical and does not appoint women on the positions where they can make decisions. This is the reason for no significant moderation. These results are in line with the literature according to which financial performance is not affected by the presence of women on board (Chong et al., 2018). Erkut and Konard (2008) revealed that there should presence of three women appointed on the board in order to get any significance regarding gender diversity and firm performance. "Bank size has a significant effect on ROAA". In this study bank size has positive impact on the bank's ROAA. The present study indicates that bank size has positive impact on ROAA. As size (Total Assets) of a bank increases it increase the ability of bank to generate higher profits. As the bank can use the total asset in various investments which in return can produce high amounts of profit for its shareholders increasing the profitability and shareholder's wealth of the bank. These findings are in line with the study of Goddard et al (2004). These findings are also supported by Onunoga (2014) who conducted an investigation upon six commercial banks located in Kenya to find out the factors that are important for profitability of banks. According to his results bank size, ownership concentration, strength of the bank as well as operating expenses positively influences a bank's profitability. The reason behind negative impact of leverage on ROAA is that increasing amount of leverage tends to lead a bank towards the bankruptcy and may cause a decrease in the returns due to high amount of interests that bank has to pay to its creditors. These results are in line with results of Sheel (1994).

In this study CIR has a negative impact on bank performance. As far as managerial efficiency is concerned it is evident from the results that CIR has a negative significant relationship with ROAA. As cost increases it tends to decrease the profits of a bank. The increase in operating expenses may lead towards bankruptcy. These results are in line with the study conducted by Zeitun (2012) who measured some factors that influenced bank's performance by conducting a study in Gulf Cooperation Council Countries during the year 2002-2009 and revealed the results that cost to income had a significant negative impact on Islamic as well as conventional banks performance. However ETA, Lev and NINC does not show any significance with ROAA. ETA has no effect on ROAA. These results are also supported by Buchory (2015). Leverage does not have any significance on returns. These results are also supported by Rob and Robinson (2009). NINC has no significance on the returns of the banks. These results are also supported by chong et al. (1996).

Table 5
Random Effects with respect to ROAA

ROAA	Coeff	Std. Error	Z	P> z	95% Conf Intervals	
POLBO	.1646367	.083234	1.98	0.048	.001501	.3277724
WBO	-1.02673	.3774514	-2.72	0.010	-1.79466	-.258805
SIZE	.2091974	.1199989	1.79	0.073	-.0195282	.4379231
ETA	.0850448	.1013952	0.84	0.402	-.1136861	.2837757
LEV	-.1610224	.0988049	-1.63	0.103	-.3546765	.0326316
CIR	-.4470584	.0992508	-4.50	0.000	-.6415863	-.2525305
NINC	.1131268	.0824028	1.37	0.170	-.0483797	.2746333
_Cons	52.53003	14.5937	3.60	0.000	23.9269	81.13316
R-Sq= 0.4513						
Prob > Chi2= 0.0000						

Note: This table demonstrates the random effect Model I with respect to Return on Average Assets.

Table 6
Moderation effect of WBO with respect to ROAA

ROAA	Coeff	Se	t	p	LLC1	ULC1
Constant	44.3551	13.2979	3.3355	.0012	17.9755	70.7347
POLBO	-.0544	.2153	-.2524	.8012	-.4815	.3728
WBO	-.1393	.2445	-.5695	.5703	.6243	.3458
Int_1	.0069	.0042	1.6453	.1030	-.0014	.0151

Note: This table demonstrates the moderation effect of women on board with respect to ROAA.

In this study board gender diversity has a positive impact on LLPT (as shown in Table 7 and 8). The presence of women on board increases the risk of the bank. This may be a result of the impositions that women are not widely represented on the positions where they can make decisions. Sometimes less competent women are appointed on boards which may result in the increased amount of risk for the firm. This study also concluded that more risk aversion does not always go in favor of the company's performance because investors with more risk aversion tend to get lower expected returns. These studies are also in line with the results of some other researches. (Jianakoplos & Bernasek, 1998). This shows that as women on board increases the overdue credit of the firm which may not be always in the favor of the firm's profitability. These results are in line with some prior studies that reveal that women are tend to be more risk averse than men (Levin et al., 1988).

In this study Leverage and NINC has a negative impact on credit risk (LLPT). CIR and Size both depicts positive impact on credit risk (LLPT). As size increases the level of risk for the firm also increases because larger size of the firm indicates large amount of credit financing. As the amount of leverage increases the risk of bankruptcy for the bank increases which shows that leverage has a negative impact on bank performance and positive significant relationship with LLPT. These results are also in line with the results of Wahyudi et al. (2019). As leverage increases the risk of the bank decreases because higher leverage means more financing and bank can utilize the finance generated through debt

financing in order to generate more profits. These results are in line with the findings of Titman and Wassels (1998). As operating expenses to total income ratio increases it increases the risk factor for the bank. As banks somehow are unable to reduce the cost to income ratio and can lead towards bankruptcy or lower amount of returns. Hence CIR is showing positive impact on the risk. Greater the CIR greater will be the risk. These results are in line with the results of Thoraneetiyana (2010). NINC has a negative impact on risk (LLPT). Non interest activities increase the return of the bank which results in more profitability and since bank does not require paying any sort of interest on this income it reduces the risk (LLPT). These results are in line with results of some other studies (Stiroh & Rumble, 2006).

Political Connections and capitalization shows no significant impact on LLPT. This study shows that board gender diversity has no significant impact on LLPT. The reason for no significant moderating effects is that the presence of women on boards of bank is very low. The Pakistani banking system is very stereotypical and does not appoint women on the positions where they can make decisions. This is the reason for no significant moderation. These results are in line with the literature according to which financial performance is not affected by the presence of women on board (Chong et al., 2018). Erkut and Konard (2008) revealed that there should presence of three women appointed on the board in order to get any significance regarding gender diversity and firm performance.

Table 7
Random effects with respect to LLPT

LLPT	Coef	Std. Error	Z	P> z	95% Conf Intervals	
POLBO	.0889209	.1187241	0.75	0.454	-.143774	.3216159
WBO	.6843426	.2613689	2.62	0.009	-.1172069	1.196616
SIZE	.0282006	.015352	1.84	0.066	-.0018888	.0582901
ETA	.1350278	.1143386	1.18	0.238	-.0890717	.3591274
LEV	-.0234665	.0076203	-3.08	0.002	-.0384019	-.0085311
CIR	.4096404	.0326857	12.53	0.000	.3455775	.4737032
NINC	.3218178	.0557791	-5.77	0.000	-.4311428	-.2124927
_Cons	-.9794587	.4130038	-2.37	0.018	-1.788931	-.1699861
R-Sq= 0.6575						
Prob > Chi2= 0.0000						

Note: This table demonstrates the random effects model 1 with respect to loan loss provisions.

Table 8
Moderation effects of WBO with respect to LLPT

ROAA	Coeff	Se	t	p	LLC1	ULC1
Constant	-.0181	.0413	-.4395	.6612	-.1000	.0637
POLBO	-.0252	.1970	-.1280	.8984	-.3657	.4161
WBO	1.6039	-.6194	.25894	.0110	.3752	2.8326
Int_1	-5.7873	3.6486	-1.5862	.1158	-13.0251	1.4506

Note: This table demonstrates the moderation effects of women on board with respect to LLPT.

5. CONCLUSION

The study investigates the impact of political connectedness of members of board and gender diversity of board on the performance of the banks. The study also focuses on identifying the moderating effect of gender diversity of board members on the relationship between bank performance and political connections of board members. The study is a big contribution towards the literature. This study is significant because of the lack of literature in the defined relationship. The banking performance is measured by using two profitability ratios (ROAA) and a Risk ratio (LLPT). The result of the study suggests that banking performance is positively influenced by political connections. This means that personal goals and objectives of members that are politically connected do not intersect with the objectives and goals as well as prosperity of the institution. Board gender diversity does not exhibit any sort of effect to mitigate or to accentuate the influence of political connectedness of BOD on performance of the banks. The results of the study revealed that politically connected board members can help to maximize bank's profitability. Women on board may increase firm's risk due to their inclusive behavior of possessing more risk aversion than men which could lead to lower expected returns. This research also identified the bank specific variables that influence the performance of the bank. The study concluded that Size of the bank (Total assets), Lev, ETA, CIR and NINC have an impact on the performance of the bank. The presence of women on board is resulting in non-profitability of banks because non competent women are being hired on the quotas that are affecting the overall performance of the bank. The study also revealed that Pakistani banking sector shows higher productivity due to the impact of political Connections which results in the better performance of the bank.

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