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# How Women Directors Decrease Cost of Capital at Family Businesses

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The decision to disclose strategy information is critical, as it reveals managerial actions, providing financial stakeholders with the information required to assess the firm's competitive advantage and performance. Disclosure might seem daunting, especially for family businesses, as it can go against the instincts of a family so closely intertwined with its business. However, depending on what is disclosed and how lenders and investors perceive it, this information affects whether the firm can borrow money, the cost and terms of that borrowing, and, ultimately whether it can attract investment.

Strategy disclosure often focuses on the firm's mission, vision, and objectives; discusses the main products, markets, and/or the competitive environment the firm operates in; and outlines specific actions taken to implement the strategy. Because this information can be highly sensitive and proprietary, the ultimate effect of strategy disclosure depends on the stakeholders' evaluation of benefits against costs. On the benefits side, by informing investors and other groups of stakeholders of their strategic plans, companies gain their trust, strengthen relationships, and ease external financing. However, strategy disclosure can backfire should it compromise the competitive advantage of the firm. Disclosing strategy information pays off when it reduces the firm's cost of capital, and this happens only when financial stakeholders feel the benefits related to strategy disclosure exceed perceived costs.

Building on these foundations, we investigated whether financial stakeholders evaluated the effectiveness of strategy disclosure differently for family firms compared to non-family firms, and whether having women on the board of directors affected their perceptions. After studying 93 Italian firms, we saw that governance arrangements, indeed, can affect the way these stakeholders evaluate costs and benefits of the strategy information disclosed.

## Challenges at Family Firms

We suspected that family business status would make strategy disclosure less effective in terms of cost of capital, which we expected would be higher for family firms than their non-family counterparts. Because family businesses may predominantly pursue non-economic goals rather than economic ones, disclosing their strategies could have a detrimental effect on the financial stakeholders' evaluation of such disclosure, with a subsequent increase in the cost of capital.

We also suspected that having a higher proportion of women directors on the board might make it easier for family firms to disclose sensitive information without increasing their cost of capital. Women's board members can be a plus for financial stakeholders who evaluate the firm's strategy. Women are perceived as mediators when conflicting goals arise in family businesses and effective communicators of the values and intangible resources of family firms. Moreover, women directors are more likely to encourage the adoption of strategic planning or managerial control systems, making family firms more professionally managed. Therefore, from the perspective of financial stakeholders, having women on the board enhances the effectiveness of strategy disclosure in family firms.

## What We Studied

The sample used in this study comprises all companies listed on Euronext Growth Milan (EGM), namely Italian SMEs with high growth potential. The initial sample includes all the 132 listed firms in 2019. After excluding firms from the financial sector, foreign/non-Italian companies, those with missing data, and outliers, our final sample consists of 93 cases.

The dependent variable, i.e., cost of capital, is defined as the weighted average cost of capital (WACC), a comprehensive measure that synthesizes the cost of debt and the cost of equity, and the data are sourced from Bloomberg database.

At each firm, we looked at the level of strategy disclosure, the family firm status, and the proportion of women directors. To measure the level of strategy disclosure, we looked at four categories:

- Corporate background information
- Corporate strategy information
- Business strategy information
- R&D information.

We prepared a checklist in which each item takes a value of 1 if the information is disclosed in the annual report or on the company website, and 0 otherwise. The strategy disclosure index is then calculated as the sum of all items disclosed by the company.

We also looked at whether the firm was family-owned and the percentage of women directors, calculated as the number of women directors relative to the board size of the company. We analyzed whether these factors affected the four types of strategy information disclosed and the firm's cost of capital.

## What We Found

The results supported our hypotheses. In general, we saw that strategy disclosure is less beneficial for family firms than their non-family counterparts, because it increases the cost of capital. However, a different picture emerges when women serve on the boards of family firms. Their presence counteracts the negative effect that being a family business has on the relationship between strategy disclosure and cost of capital. In other words, having women directors appears to make strategy disclosure more effective at family firms, as an increasing number of women directors translates for family firms into a smaller increase in the cost of capital, compared to similar non-family firms. Interestingly, when a critical mass of women directors is appointed (i.e., at least three women), they offset the negative effects of the family firm status to the extent that, even for this group of companies, strategy disclosure actually helps them reduce the cost of capital.

## Takeaways

Our research offers several key takeaways.

First, strategy disclosure is generally not beneficial for family businesses since, unlike their non-family counterparts, it is associated with an increase in the cost of capital. Family business owners, managers, or advisors should thus recognize that making strategy information available to the market can significantly impact financial stakeholders' assessment and decisions, particularly in companies where family logic may prevail.

Second, the way financial stakeholders perceive and assess strategy information is affected by the board gender diversity. Increasing the number of women directors helps make strategy disclosure more beneficial for family businesses. When the presence of women is large enough to represent a critical mass, the benefits of strategy disclosure outweigh its costs, and the negative relationship observed between strategy disclosure and cost of capital is reinstated for family businesses.

Third, regulators and policymakers should encourage higher women participation, promoting and endorsing legislations aimed at increasing women's representation on the board of directors. In this respect, the results of this study can help rationalize the interventions of some European countries like Norway or Germany where initial laws on board representation have been enacted.

## Explore the Research

Strategy disclosure and cost of capital: The key role of women directors for family firms (https://www.sciencedirect.com/science/article/abs/pii/S1877858523000190) , Journal of Family Business Strategy, June 2024

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