Taking the Lord's Name in Vain: The Impact of Titled Directors on 19th century British Banks[1]

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ABSTRACT

This paper utilizes data on the presence of prominent individuals—that is, those with political titles (e.g., Members of Parliament) and those with aristocratic titles (e.g., lords)--on the boards of directors of British banks from 1879-1909 to investigate whether the appointment of well-connected directors enhanced equity value for bank shareholders. Our analysis of panel data shows that the appointment of well-connected directors to the boards of directors did not increase the rate of return on bank equity. In fact, we find that the appointment of MPs to directorships had *negative* effects on bank equity. Our event-study analysis corroborates this finding, showing that bank shares exhibited *negative* abnormal return when their directors were elected to Parliament. Taken together, our results indicate that well-connected directors yielded little--or even negative--economic payoff to bank shareholders in pre-war Britain. We speculate that such appointments were a form of costly "prestige consumption" on the part of banks.

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selection may be based on unobservable factors, since weak or otherwise struggling banks may have been more likely to appoint titled directors.

To better identify causality, we exploit the time dimension of the panel data (i.e., some banks appointed connected directors while others remained unconnected during the sample period) and estimate the effects of connected directors via differences-in-difference methods as follows:

$$Ln(Assets_{it}) = \beta_i + \beta_t + \beta_1 MP_{it} + \beta_2 Noble_{it} + \varepsilon_{it}$$
$$Ln(Assets_{it}) = \beta_i + \beta_t + \beta_1 Connected_{it} + \varepsilon_{it}$$
$$Return_{it} = \beta_i + \beta_t + \beta_1 MP_{it} + \beta_2 Noble_{it} + \varepsilon_{it}$$
$$Return_{it} = \beta_i + \beta_t + \beta_1 Connected_{it} + \varepsilon_{it}$$

Note that the bank fixed effects coefficient, β_i controls for bank-specific factors that are more or less constant over time, and the year fixed effects coefficient, β_t, captures economy wide shocks that affect all banks. Hence, by including both bank fixed effects and year fixed effects, we are comparing a change in bank performance before and after the appointment of connected directors relative to a statistical benchmark (i.e., a change in the performance of banks which remained unconnected) in a given year.

Table 5 reports the results of these panel regressions. The coefficient on the presence of MP directors in the equation for bank size is positive and significant (column 1), suggesting that banks were larger after the appointment of connected directors. The coefficient on the presence of noble directors is negative but insignificant (column 1). The results with the number of connected directors yield qualitatively similar results (columns 3 and 4), although the coefficient on the number of MP directors is not statistically significant. The results on dividend-adjusted returns provide no evidence to suggest that bank performance improved after the addition of connected individuals to the board of directors. On the contrary, the performance seems to deteriorate when banks appointed MPs (column 5). We observe similar patterns when we use the number of MP directors as a proxy of political connections instead of a dummy for their presence, suggesting that as the number of MP directors increased, dividend-adjusted returns tended to decline (column 7). In sum, we find evidence that political connections are associated

Table 2: Year-by-year cross-sectional regression (dependent variable, dividend-adjusted return)

Panel A

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)	(14)	(15)	(16)	(17)
VARIABLES	1879	1881	1883	1885	1887	1889	1891	1893	1895	1897	1899	1901	1903	1905	1907	1909	Pooled OLS
Presence of Connected Directors	0.152**	0.0195	-0.0389	0.00668	0.138*	0.0807*	-0.0358	0.0162	0.0328	-0.136	0.0391*	-0.0166	0.00527	-0.0168	-0.0974	-0.0696***	0.0140
	(0.0602)	(0.0368)	(0.0668)	(0.0189)	(0.0814)	(0.0452)	(0.0285)	(0.0228)	(0.0226)	(0.137)	(0.0212)	(0.0243)	(0.0248)	(0.0185)	(0.0685)	(0.0240)	(0.0152)
Constant	0.00178	0.0685**	0.0746***	0.105***	0.185***	0.0292	0.0504***	0.0976***	0.149***	0.0776*	0.0244*	0.0810***	0.0773***	0.0597***	0.109***	0.0818***	0.0339
	(0.0445)	(0.0292)	(0.0224)	(0.0138)	(0.0215)	(0.0347)	(0.0132)	(0.0100)	(0.0127)	(0.0431)	(0.0139)	(0.0161)	(0.0220)	(0.0158)	(0.0291)	(0.0163)	(0.0366)
Observations	86	90	93	93	83	80	78	78	72	65	58	49	47	39	34	31	1,076
R-squared	0.038	0.001	0.006	0.001	0.062	0.025	0.023	0.007	0.025	0.026	0.048	0.009	0.001	0.023	0.051	0.224	0.065

Panel B

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)	(14)	(15)	(16)	(17)
VARIABLES	1879	1881	1883	1885	1887	1889	1891	1893	1895	1897	1899	1901	1903	1905	1907	1909	Pooled OLS
Presence of MP directors	0.159***	0.0152	-0.0392	0.00576	0.0441	0.0851*	-0.0376	0.00851	0.0384	-0.187	0.0234	-0.00294	0.00973	-0.0210	-0.132	-0.0508**	0.00262
	(0.0561)	(0.0382)	(0.0757)	(0.0191)	(0.0463)	(0.0469)	(0.0272)	(0.0255)	(0.0232)	(0.163)	(0.0208)	(0.0244)	(0.0238)	(0.0170)	(0.0898)	(0.0238)	(0.0155)
Presence of Lord Directors	-0.0836	0.0265	-0.0345	0.0238	0.366	0.00525	-0.0395	0.0495	-0.0417**	0.0926	0.118***	-0.0335	-0.0130	-0.0107	0.0364	-0.0508	0.0280
	(0.155)	(0.0229)	(0.0447)	(0.0257)	(0.326)	(0.0469)	(0.0574)	(0.0370)	(0.0160)	(0.0592)	(0.0338)	(0.0381)	(0.0288)	(0.0195)	(0.0502)	(0.0344)	(0.0313)
Constant	0.00582	0.0683**	0.0749***	0.105***	0.191***	0.0328	0.0515***	0.0976***	0.150***	0.0759*	0.0244*	0.0798***	0.0785***	0.0620***	0.0954***	0.0754***	0.0353
	(0.0444)	(0.0289)	(0.0223)	(0.0137)	(0.0225)	(0.0340)	(0.0131)	(0.0101)	(0.0127)	(0.0429)	(0.0141)	(0.0159)	(0.0216)	(0.0150)	(0.0297)	(0.0161)	(0.0367)
Observations	86	90	93	93	83	80	78	78	72	65	58	49	47	39	34	31	1,076
R-squared	0.037	0.002	0.006	0.003	0.128	0.023	0.031	0.015	0.036	0.045	0.103	0.017	0.006	0.044	0.097	0.178	0.065

Robust standard errors in parentheses

*** p<0.01, ** p<0.05, * p<0.1

Table 4: Year-by-year cross-sectional regression (dependent variable, dividend-adjusted return)

Panel A

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)	(14)	(15)	(16)	(17)
VARIABLES	1879	1881	1883	1885	1887	1889	1891	1893	1895	1897	1899	1901	1903	1905	1907	1909	Pooled OLS
Number of Connected Directors	0.103***	0.0227	-0.00558	0.00688	0.0853	0.0461*	-0.0260	0.0156	0.0141	-0.0911	0.0255**	-0.0130	0.000627	-0.0117	-0.0176	-0.0421***	0.00851
	(0.0352)	(0.0232)	(0.0456)	(0.0128)	(0.0542)	(0.0235)	(0.0167)	(0.0189)	(0.0118)	(0.0870)	(0.0122)	(0.0193)	(0.0122)	(0.00844)	(0.0165)	(0.0138)	(0.00952)
Constant	0.00469	0.0663**	0.0666***	0.105***	0.196***	0.0346	0.0494***	0.0975***	0.153***	0.0750*	0.0260*	0.0812***	0.0792***	0.0608***	0.0697*	0.0785***	0.0345
	(0.0423)	(0.0284)	(0.0227)	(0.0134)	(0.0221)	(0.0327)	(0.0128)	(0.00991)	(0.0122)	(0.0434)	(0.0135)	(0.0154)	(0.0196)	(0.0137)	(0.0387)	(0.0145)	(0.0364)
Observations	86	90	93	93	83	80	78	78	72	65	58	49	47	39	34	31	1,076
R-squared	0.041	0.004	0.000	0.002	0.037	0.019	0.023	0.008	0.011	0.027	0.042	0.012	0.000	0.042	0.007	0.269	0.065

Panel B

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)	(14)	(15)	(16)	(17)
VARIABLES	1879	1881	1883	1885	1887	1889	1891	1893	1895	1897	1899	1901	1903	1905	1907	1909	Pooled OLS
Number of MP directors	0.121***	0.0223	-0.00143	0.00387	0.0290	0.0494**	-0.0254	0.00941	0.0211	-0.131	0.0187	0.000126	0.00235	-0.0127	-0.0369	-0.0362**	0.00532
	(0.0424)	(0.0285)	(0.0521)	(0.0132)	(0.0338)	(0.0244)	(0.0169)	(0.0206)	(0.0132)	(0.108)	(0.0116)	(0.0176)	(0.0121)	(0.0102)	(0.0426)	(0.0139)	(0.0115)
Number of Noble Directors	-0.0865	0.0242	-0.0360	0.0245	0.367	0.0153	-0.0360	0.0498	-0.0463**	0.114	0.118***	-0.0482	-0.00585	-0.00845	0.0105	-0.0482**	0.0137
	(0.151)	(0.0224)	(0.0458)	(0.0262)	(0.325)	(0.0451)	(0.0396)	(0.0369)	(0.0178)	(0.0759)	(0.0336)	(0.0340)	(0.0222)	(0.0145)	(0.0303)	(0.0225)	(0.0244)
Constant	0.00745	0.0663**	0.0669***	0.105***	0.194***	0.0361	0.0507***	0.0973***	0.152***	0.0734*	0.0237*	0.0817***	0.0795***	0.0608***	0.0694*	0.0782***	0.0350
	(0.0428)	(0.0286)	(0.0229)	(0.0135)	(0.0217)	(0.0332)	(0.0129)	(0.00999)	(0.0123)	(0.0436)	(0.0136)	(0.0156)	(0.0199)	(0.0138)	(0.0398)	(0.0148)	(0.0364)
Observations	86	90	93	93	83	80	78	78	72	65	58	49	47	39	34	31	1,076
R-squared	0.042	0.004	0.001	0.003	0.126	0.019	0.031	0.016	0.023	0.048	0.110	0.054	0.001	0.043	0.021	0.277	0.064

Robust standard errors in parentheses

*** p<0.01, ** p<0.05, * p<0.1

Table 5: Effects of connected directors on bank size & dividend-adjusted return (differences-in-difference)

VARIABLES	(1) size	(2) size	(3) size	(4) size	(5) return	(6) return	(7) return	(8) return
Presence of MP directors	0.0610*				-0.0441*			
	(0.0361)				(0.0225)			
Presence of Noble Directors	-0.0666				0.0191			
	(0.0585)				(0.0365)			
Presence of Connected Directors		0.0329				-0.0203		
		(0.0356)				(0.0199)		
Number of MP directors			0.0462				-0.0296*	
			(0.0298)				(0.0167)	
Number of Noble Directors			-0.0637				0.00692	
			(0.0466)				(0.0312)	
Number of Connected Directors				0.0248				-0.0196*
				(0.0255)				(0.0118)
Constant	14.28***	14.28***	14.28***	14.28***	0.0508	0.0469	0.0503	0.0484
	(0.0452)	(0.0446)	(0.0441)	(0.0438)	(0.0361)	(0.0362)	(0.0357)	(0.0356)
Observations	1,265	1,265	1,265	1,265	1,076	1,076	1,076	1,076
R-squared	0.608	0.605	0.609	0.606	0.074	0.071	0.074	0.072
Number of Banks	139	139	139	139	114	114	114	114

Robust standard errors in parentheses
*** p<0.01, ** p<0.05, * p<0.1

Table 7: Effects of politically connected directors on dividend-adjusted return with controls (differences-in-difference)

VARIABLES	(1) return	(2) return	(3) return	(4) return	(5) return	(6) return
Presence of MP directors	-0.0431*		-0.0534*		-0.0739**	
	(0.0240)		(0.0299)		(0.0363)	
Presence of Noble Directors	0.0211		0.00111		0.0173	
	(0.0373)		(0.0358)		(0.0374)	
Number of MP directors		-0.0285		-0.0351*		-0.0513**
		(0.0176)		(0.0188)		(0.0241)
Number of Noble Directors		0.00807		-0.00962		0.00157
		(0.0319)		(0.0314)		(0.0325)
Total number of directors	0.000613	0.000609	0.00261	0.00257	5.67e-05	4.63e-05
	(0.00301)	(0.00314)	(0.00266)	(0.00276)	(0.00262)	(0.00291)
Lagged return	-0.0274	-0.0261	-0.00744	-0.00614	-0.0156	-0.0141
	(0.0233)	(0.0234)	(0.0217)	(0.0218)	(0.0221)	(0.0224)
Log(Assets)			-0.0830*	-0.0854*	-0.000625	-0.00250
			(0.0498)	(0.0492)	(0.0446)	(0.0444)
Loan-to-Asset Ratio			0.370*	0.379*	0.372	0.385
			(0.222)	(0.226)	(0.254)	(0.260)
Cash-to-Asset Ratio			0.490	0.487	0.506	0.505
			(0.449)	(0.451)	(0.509)	(0.513)
Age					4.42e-05	-6.31e-06
					(0.00258)	(0.00259)
Constant	0.0465	0.0463	0.964	0.994	-0.246	-0.224
	(0.0420)	(0.0426)	(0.738)	(0.728)	(0.645)	(0.643)
Observations	1,042	1,042	935	935	762	762
R-squared	0.076	0.075	0.116	0.116	0.105	0.105
Number of Banks	113	113	109	109	85	85

Robust standard errors in parentheses
*** p<0.01, ** p<0.05, * p<0.1