Effect of Corporate Governance on Firm Performance on Modarba Companies of Pakistan: A Case Study of Top 5 Companies

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Abstract
In the decades or so there is many global financial crises that capture the attention of corporate governance in the whole world it is moral duty conform by law and showing ethics.so the country like Pakistan a developing country can used as a tool for financial performance. The study shows the impact of corporate Governance on firm performance of modarba companies of Pakistan. we can take top 5 companies of the industry from the period of 2011 to 2015. we can take board size, CEO duality, board committees, and board independence, as independent variable and ROA and ROE as dependent variable.

After the research of that we find that overall corporate governance variable have significant impact on firm performance. There is no relationship between board size and all dependent variable. Board independence has positive and strong relationship on all variable However, there is negative correlated between CEO duality and all dependent variable but significantly related to ROA

Keywords: corporate governance, financial performance, firm performance

Introduction
Every organization want become leader of the market but only those organization is consider leader who can make perfection in all department. In every organization human resource is consider as a backbone of the company. Not only backbone of a company but also play a vital role in development and sustainability. In a situation when competitor is difficult then it tell us way who to play the game. Corporate governance now becomes an important part in the last two decades. In recent years we can see many accounting scandal and frauds that can affect the biggest companies of the world. In the modern world we can say that corporate governance play a vital role in firm sustainability in long term and increasing interest of researcher and policy maker through analysis and practices. A literature can also show the many accounting fraud in the past

By using as a tool corporate governance supplier of capital save their investment for yourself. (Shleifer and Vishny, 1997).Shareholder are the people who take part in contributing the money and special corporate governance cycle help them to apply control over the management of the company for the maximization of the shareholder wealth. The BOD act as an agent for reducing the agency cost (Fama and Jensen, 1983).

This research shows the empirical analysis to test the effect of corporate governance phenomena on firm performance on listed top 5 modarba companies of Pakistan for the last five year 2011-
2015 firm performance is calculated through profitability that is return on equity (ROE). The return on equity is a measure of the company's profitability. It is calculated by dividing the net income of the company by the average shareholders' equity over a period of time. ROE is an important metric for evaluating a company's financial performance. A higher ROE indicates that a company is generating more profit relative to its shareholders' equity. ROE is calculated using the formula:

\[ \text{ROE} = \frac{\text{Net Income}}{\text{Shareholders' Equity}} \]

**Literature Review**

**Link between board of director and Firm performance**

Board of director are representative of the all the shareholder and stakeholder of the company. The company delegated with the responsibility of checking the performance and activities of the top management to ensure they work for the best interest of the shareholder. Sometime board vested our power and not done their responsibilities. The board of a company is one of the cores internal corporate system (Brennan, 2006). The problem of structure of the board of director as a corporate governance system has received significant attention in last decade from studies market practices and regulators. It continues to take attention because theory provides different view on impact of board structure on the control and performance of firm on the other hand empirical evidence is unsatisfying.

**Effect of Board Size on Firm Performance**

This is the most important feature of the board structure. After review the literature we saw that two different views on factors effect on board size on firm value the first say larger board is effective in performance of the company. And there is positive impact of board size with the firm value (Elkholya, 2009; Klein, 2002; Dalton et al., 1999). It is seen that strong arguments in support of larger board size one thought is larger board gave a verity it is obviously that when there is more people in the pool then their knowledge is more and person from every field is make the decision more strong and reliable for the company (Dalton et al., 1999; Pearce and Zahra, 1992). When there is more people involve in the company then more external linkages (Goodstein et al., 1994).

The other school of thought is who say larger board show less efficiency in the performance of the company. Many studies shows there is negative relationship between size and performance of company(Yermack, 1996; Eisenberg et al., 1998; Cheng, 2008 Bonney, 2004). A study show there is negative association between size with firm under some critical factor. Many scholar say large board is ideal. On the other hand in larger board there is lack of communication between board member (Jensen, 1993) the biggest problem of larger board is small group and all having own interest that will cause less efficient decision. It is also a problem that decision is taken quite slowly.

**Effect of board independence on firm performance**

Board independence mean board is take decision without any pressure of any person within the organization. When non-executive director are part of board then board is more independent (John and Subnet, 1998) but how it is connected with company performance but the problem is here is that executive director is more close with the actives of the organization then the non-executive director however the non-executive director work as a consultant or advisory role for the maximize the shareholder wealth and protect the Interest of shareholder and stakeholder of the company (Fama, 2000), but some researcher found there is no significant relation between nonexecutive director and company performance (Babat and Black, 2002).

It shows that the effectiveness of a board depends on the mixture of Executive and non-executive director of the company.

**Effect of CEO Duality on firm performance**

It is quite controversial that companies CEO and chairman is a same person or not. There are some example that shows advantages and disadvantages of change person of CEO and chairman like combination of two position CEO and chairman makes greater power to the CEO (Brickley, et al 1997). We can see that CEO take charge of chairman after good performance among collage and say it is the reward for the good performance in the conflict of outside directors. In this situation separate the CEO and chairman however, giving the duties of CEO and chairman to one person is quite hard for the board to replace a poorly performing CEO, which show the less flexibility of a board and result decrease in performance (Goyal et al., 2002).

In CEO-chairman duality, CEO is performing dual role of chairman and CEO there are two schools of thought. First say if there is same person in CEO and chairman than he make own paper for exams. Segregation of duties leads to (1) Independence establishes (2) Chairman gave order to CEO (3) Monitoring OF board activities (Baysinger and Hoskisson, 1997). But on the other side there is some researcher who believes that CEO and chairman should be same person. If there is same person on CEO and chairman position than they find (1) strong leadership (2) strong internal efficiency (3) end of conflict between CEO and chairman (Davis, Schoorman and Donaldson, 1997).

**Conceptual Framework**

![Conceptual Framework Diagram](image)

**Hypotheses**

H1: Board size has impact on ROA On modarba companies
H2: Board committee has impact on ROA on modarba companies
H3: Board independence has impact on ROA on modarba companies
H4: CEO duality has impact on ROA on modarba companies
H5: Board size has impact on ROE on modarba companies
H6: Board committee has impact on ROE on modarba companies
H7: Board independence has impact on ROE on modarba companies
H8: CEO Duality has impact on ROE on modarba companies

**Reach Design**

The purpose of this study is to know the effect the corporate governance on firm performance in modarba companies of Pakistan in the last 5 years. This section tells us about research method and tests the hypotheses that written above. The qualitative approach which is most well-known method to determine the relationship between variables.

**Sampling Data Sourcing and Collection**

This research is conducted on top 5 listed modarba companies of Pakistan. It is qualitative study. The sampling period is decided between 20011-2015 we can used secondary data collected from their websites. The sample size is 5 because of it is a case study. The cross sectional data can be used. The companies which we include in the study they have debt in capital.

**Variable Descriptions**

Corporate governance is considered as independent variable and firm performance is chosen as dependent variable. The proxy measure of corporate governance is board size, board independence, board committee and CEO duality. The firm performance is measured through return on asset (ROA) and return on equity (ROE).
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Measurement of Variable

<table>
<thead>
<tr>
<th>Variable</th>
<th>Name</th>
<th>Measurement</th>
</tr>
</thead>
<tbody>
<tr>
<td>BOSIZ (IV)</td>
<td>Size of board</td>
<td>Total member in board</td>
</tr>
<tr>
<td>BOIND (IV)</td>
<td>Board Independence</td>
<td>Non-executive member over total member</td>
</tr>
<tr>
<td>BOCOM (IV)</td>
<td>Committees in board</td>
<td>Total committee</td>
</tr>
<tr>
<td>CEO(DV)</td>
<td>Same person</td>
<td>Chair or CEO if one person than 1 if change person than 0</td>
</tr>
<tr>
<td>ROA(DV)</td>
<td>Return</td>
<td>Income divide by book value of asset</td>
</tr>
</tbody>
</table>

The analysis starts with examining the basic characteristics of the data like mean, median, maximum value, minimum value, standard deviation, skewness and kurtosis, etc. In the given below, we discuss these things of the data period from 2011 to 2015.

<table>
<thead>
<tr>
<th>Variable</th>
<th>Coefficient</th>
<th>Standard E</th>
<th>T-Stat</th>
<th>Pro.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Constant</td>
<td>0.285181</td>
<td>0.145925</td>
<td>1.95429</td>
<td>0.0000</td>
</tr>
<tr>
<td>BODCOMM</td>
<td>0.013262</td>
<td>0.010860</td>
<td>1.22125</td>
<td>0.2225</td>
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<tr>
<td>BODINDEP</td>
<td>0.199892</td>
<td>0.099271</td>
<td>2.01360</td>
<td>0.0445</td>
</tr>
<tr>
<td>BODSIZE</td>
<td>0.002139</td>
<td>0.002893</td>
<td>0.73950</td>
<td>0.4599</td>
</tr>
<tr>
<td>CEO(DV)</td>
<td>0.045885</td>
<td>0.024081</td>
<td>-1.90542</td>
<td>0.0572</td>
</tr>
</tbody>
</table>

Descriptive

The mean of the board committee is 2.25 and the minimum value is 0 and maximum is 5 so there is week presence of compliance. The mean of CEO duality is 0.21 with the maximum of 1 and minimum of 0. So there is different person on most of the sample companies. Board independence has a mean of 0.639. its range from 0 to 1. that shows there is non-executive member in the board. Board size has a mean of 7.97 with the minimum of 3 and maximum value is 16. if the size of board is greater than 5 that means good.

The average of ROA is 6.5% and the average of ROE is 11%. both show the positive number that is good during the year 2011 to 2015. If it shows negative sigh than that is economic down fall.

This test is used to check the problem of is there is a problem of multicollinearity or not to know the relationship between the all dependent variables. This problem will be occur when two or more independent are strong correlated with each other so it is essential to check the multicollinearity.
The effect of board independence is found the most significant variable since t is positively to all measure however good corporate governance practice decrease corporate issue with the help of non-executive directors in the monitoring and auditing process the large amount of committee is increase the profit than who have less board committee In the last if the person of Ceo and chairman is not same than they can earn more profit rather than same person as the show in the result there is negative correlated with all measure to protect interest of shareholder and maximize the shareholder wealth

### Reference


