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Impact of Corporate Governance on Firm's Performance: A Case of Micro-Financing Institutions in Sialkot, Pakistan

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ABSTRACT

This research paper attempts to evaluate the relationship between corporate governance and performance of the microfinance institutions in Sialkot employing primary source of data. A representative sample of 80 respondents from the top-level management such as board of directors, chief executive officers, managing directors and all the related staff who are responsible for the growth and progress of the microfinance institutions was selected using stratified random sampling technique. The findings of the study revealed that the CEO duality, board independence and ownership structure were the significant variables affecting the firm performance whereas the variables (board size and audit committee independence) showed insignificant impact. The analysis of the research suggested that micro finance institutions should have good and solid governance framework in order to enhance decision making and minimize the possibilities of the management failures ultimately improvement in the firm's performance.

Key Words: Corporate governance, board size, CEO duality, board independence.

1. Introduction

The financial practitioners and economists emphasize that the development of the financial service sector is a key for the economic development of a country and the economic well-being of its people as it supports people to smooth their income and increase their investment opportunities (Aftab & Naveed, 2013). It drastically makes effects on social, political and economic environment of the country. Thus, country should have good financial systems in order to offer the appropriate access for the people in getting money in order to bring improvement in the living standards. However, it has been analyzed that

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number of people who are not accessible to the financial services, especially in the developing countries (Burkart et al., 2014).

Significance of corporate governance in any organization, especially, microfinance institutions cannot be neglected at any instance, especially in the development, welfare, social justice, economic wellbeing to its people (Coles et al., 2008). Good corporate governance provides health and education facility to its participants on the equal basis which directly and indirectly helps the country to increase the sector of development (Thrikawala et al., 2013). Pakistan is struggling since independence and under the process of being run under the system of cooperative governance (Knoll & Zloczysti, 2012).Corporate governance of the country or company is either based on good governance or bad governance. Good corporate governance is based on strengthening, effectively managing and controlling the organizational management functions, strong decision-making powers, and achievements of microfinance institutions (MFIs) to accomplish their primary objectives. The primary objectives promote further development of industry that have been asserted key element as considered to determine MFI performance (Ault, 2016; Tiruneh, 2015). The main functions of the corporate governance are to assign these power decisions amongst those people who work for the development of microfinance institutions (Carney, 2005).

The performance indicator of the microfinance institutions is interlinked with the corporate governance. Main aim is to develop the economic conditions, improve the way of living standards, control inflation rate, and control the rate of unemployment and other related tasks and activities which all are made for the progress of economy through integration of good corporate governance (Fan et al., 2007; Chakrabarty and Bass, 2013). It is observed that the microfinance institutions are considered as the sensitive institution where the role of the top management is very important in the progress of the organization. The main aim of these institutions is to accommodate the poor people of Pakistan and make them financial stable through providing these services, and also support the innovative activates in the country (Archera and Jones-Christensen, 2011; Mumi et al. 2018). The role of the board of directors, shareholders, stakeholders and managing directors is considered as the top management of the organization is very important (Hussain,2003). All the main power and authority for the implementation of policy and decisions are in the hands of the executives. With the passage of time, they all are transformed from top level to middle level of the organization (Javid & Iqbal, 2008).

Poor governance is always acting opposite in direction as compared to good governance. Good corporate governance has become important due to effectively managing demands for reflecting transparency and accountability of fund effectively utilized to well perform microfinance activities (Chen & Yi, 2008). Effective corporate governance has a pivotal role in improving the financial performance of the firm. Sialkot city was chosen purposively due to its emerging entrepreneurial and trade importance. Many micro finance institutions are operating in this industrial city and the relationship between corporate governance and performance of micro finance institution should be assessed. As the research in hand revolves around the main questions as: To what extent board size and audit committee independence has impacts on the firm's performance? To what extent, the board independence and CEO duality has impacts in terms of strengthening of the corporate governance and how does it lead to the strong corporate performance? What is the role of the ownership structure in terms of the corporate governance and overall enhancement of the corporate performance? Thus, this study is focused to determine the important factors effecting performance of micro finance institutions in district Sialkot. The rest of the paper is structured as follows: section represents review of literature, third section entails research methodology, section four describes discussion and last section is about conclusion.

2. Literature Review

Corporate Governance is a very established concept from the past two decades and now days because of its comparative importance in the performance of the overall firm. Need for corporate governance arises when scandals came out because of the financial crises of Enron, WorldCom etc. Javid & Iqbal (2008) studied that the contribution of the Corporate Governance variables such as board size, CEO duality, educational level of the board members, ownership structure, experience of board members and board ownership towards the performance of the financial institutions. They also revealed the negative relationship between CEO duality, board size and board Ownership and the firm's performance but the positive relationship between the board educational level and experience, audit committee independence, board independence and the firm's performance. Jegatheesan et al. (2011) stated that the microfinance was the provision that gave access to different financial services like remittances, credit, micro insurance, savings, leasing to low-income clients including customers and the self-employed who usually having lack of access to the banking and relevant services. Its main aim was to offer an eternal access to appropriate financial services having savings, fund transfer and insurance. Micro finance became more extensively accepted and moved into the main stream and the provision of services to the poor might also be escalated, improved the efficiency and outreach while keeping the costs to be lowered.

Corporate governance term transpires due to the consequent relationship between the governance of corporations and the governance of countries or nations (Knoll & Zloczysti, 2012). The firmness of this relationship is derived from the fact that as governance of any country plays a vital role in the performance of the whole economy of the country just like governance of corporations also plays a very imperative role in the performance of the corporation as well in the performance of overall economy. This section of literature review presents past research works and theories that have been conducted by the past researchers in the domain of highlighting the significance of corporate governance and how does it impact on the performance of the microfinance institutions. Corporate governance basically comprises of two mechanisms i.e. internal corporate governance and external corporate governance. Internal corporate governance works on the mechanism of preservation of shareholder's concern and monitoring the top management by the board of directors whereas external corporate governance works on the mechanism of observing and directing managers with the help of laws and regulations and governing many parties involved such as stakeholders and professional institutions (Thrikawala et al., 2013). The performances of the corporate governance are evaluated in number of terms like the return on investment, assets, and assign power to those people who are qualified and have skills to run the setup of microfinance institutions, profitability and development of the microfinance institutions (Blanchflower, 2014). It is true that the current condition of Pakistan is considered as the developing country and need a lot of investment to make its population strong and healthy. Today, the current condition of the corporate governance of Pakistan is not up to the mark, due to so many reasons like, inflation rate, unemployment, energy crises; transportation system is not working properly and many other related issues that affect the decisions of corporate governance (Galema et al., 2012).

The process of the top management leadership styles and commitment towards the work plays an important role in the development of the microfinance institutions. The corporate governance supports the microfinance institutions so that they can become helpful for the lower-class people of Pakistan. Obtaining the top management leadership and commitment plays a critical role for the diversification programs to succeed (Sami et al., 2011). This is one of the best ways for the commitment and communication of all the employees working in the microfinance institutions. Corporate governance established their corporate offices and committees that coordinate the microfinance work force diversity and provide the feedback to top management. Wong and Chen (2014) revealed the influence of the corporate governance tool on the firm's performance. They identified that board size, CEO Duality and deviation from the voting right and cash flow right is negatively related to the firm's performance whereas board independence and insider ownership contributes positively towards the firm's performance. The role of the corporate governance is very important to evaluate the performance of the microfinance institutions. Lensink et al. (2018) examined the effect of microfinance having synchronized combination of the financial & nonfinancial services and corporate governance on the performance of microfinancing institutions. Employing the global data set of microfinancing institutions in seventy-seven states, they found that the endowment of nonfinancial services did not affect nor change microfinancing institutions' financial sustainability and efficacy. However, the outcomes recommended that the provision of these social services was attached with the modified loan quality and higher depth of outreach activities.

On the behalf of the feedback board of directors takes all the effective and important decisions that can benefits the organization. It is fact that the work of managing diversity cannot be done without the top management. Most of the microfinance institutions are also based on the advisors' groups or tasks work forces to monitor the policy and procedures of the organization (Peng et al., 2013). Microfinance institutions are directly impact on the diverse group within the organization and take the decisions on the base of the feedback and suggestion to the top management of the microfinance institutions.

2.1 Research Gap

Radical Feminism and feminist views the world through the eyes of man and that patriarchal structure is the most important element in women's oppression, thus eliminating all other forms of gender discrimination from the society like; race, culture, caste and class. Radical feminist believes that the oppression of women by men is so deeply rooted in society that a complete overhauling of the society is needed in order to attain equality for women. Radical form of feminism focuses on society and ideology to be the main cause for the subjugation of women. It was the extreme women's activist who gave the major hypothetical meaning to women's liberation and it is radical woman's rights that has filled in as the reason for motivation and investigation directing women around the globe.

3. Research Methodology

Research methodology plays a very important role in completion of study. Research methodology indicates the research methods and tools in the research work. The research methodology comprises of various phases, initiating from the development of research problem to the interpretation and reporting.

3.1 Data Collection Technique

Keeping in view the research objectives, we collected the primary data based on well structure questionnaire. The primary data was collected by doing face to face interviews of the selected respondents

3.2 Sampling Frame and Sample Size

Information were collected from top-level management, such as board of directors, chief executive officers, managing directors and all the related staff who are responsible for the growth and progress of the microfinance institutions. The data were collected through stratified random sampling from 80 respondents of three microfinance institutions working in district Sialkot, Pakistan. These institutions were Tameer Microfinance Bank, Apna Microfinance Bank Ltd and Khushhali Microfinance Bank Limited.

In this study, the researcher used three microfinance institutions such as Tameer Microfinance Bank, Apna Microfinance Bank Ltd and Khushhali Microfinance Bank from Sialkot city itself.

3.3 Data Analysis Technique

In this context, the regression analysis was applied to identify and analyze the relationship between the variables of corporate governance and the performance of micro financing institutions.

3.4 Theoretical Framework

Framework model of paper is designed and developed under the strong consideration of past and similar literature, model and theory which directly support corporate governance and performance relationship in context of Microfinance Institutions. In according to framework model of paper is composed of two variables. These variables are independent and dependent. Independent variables are board-size, audit committee independence, CEO duality, board independence and ownership structure, whereas dependent variable is firm performance evaluated in terms of market value of microfinance institutions working in Pakistan. Explanation of these variables is given as:

I. Broad Size

Board comprises of the group of the directors is the group of the individuals, that are elected for the representation of the stockholder. Mandate of the board is establishment of policies and procedures for the corporate management as well as making the decisions on main company problems and issues. It will be taken in number as the size of the board is highly dependent on the size of the company (Peng, Au, & Wang, 2013). It is also recommended by the studies of Javid & Iqbal (2008) and Wong and Chen (2014).

II. Audit Committee Independence

Audit committee is considered as the opening committee of the board of the director's company that is in charge of the overseeing the financial reporting as well as disclosure. All companies should maintain the qualified the audit committee so that it can be listed on the stock exchange. In our research we have taken this variable in dummy form if audit committee exists then one (yes) otherwise zero (no.) This variable is not mainly used in various researches. The contribution of this variable is checked by the study of Javid & Iqbal (2008).

III. CEO Duality

CEO duality is considered to situation when CEO also tends to hold position of chairman of board. Board of the directors that is set up for the monitoring of the managers that CEO on behalf of shareholders (Thrikawala et al., 2013). We took this variable in dummy form if CEO duality exists then one (yes) otherwise zero (no.) This variable has been used in research studies of Javid & Iqbal (2008) and Wong and Chen (2014).

IV. Board Independence

Board is independent is deliberated as the corporate board that majority of the external directors who are considered to be not affiliated with firm's top executives and have minimum dealing with organization in avoiding of the conflicts of the interests. In our research we have taken this variable in dummy form if board independence exists then one (yes) otherwise zero (no.) This variable has been used in research studies of Javid & Iqbal (2008) and Wong and Chen (2014).

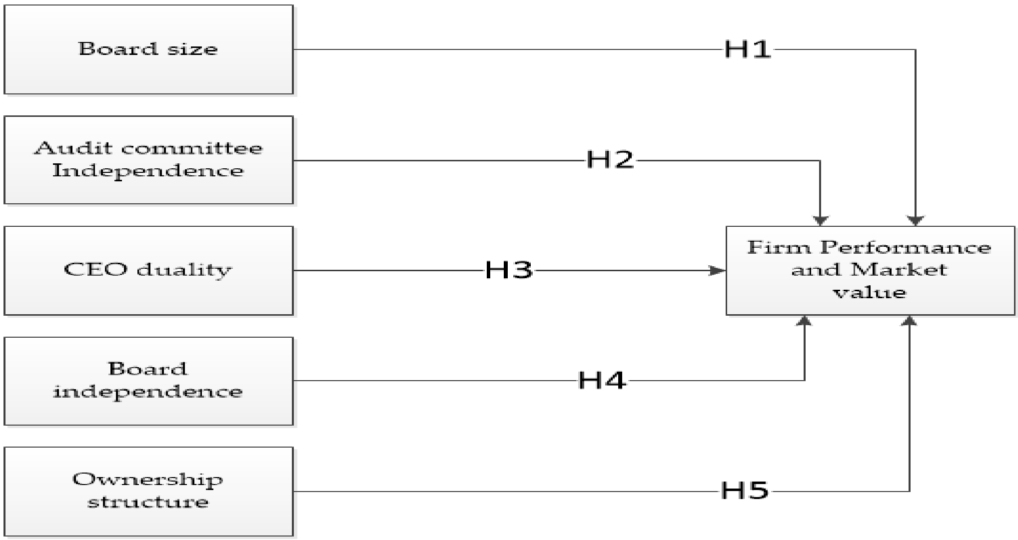
V. Ownership Structure

For number of the new businesses, best beginning ownership structure is the either sole proprietorship or partnership (Sami et al., 2011). This variable is taken as dummy variable as if ownership structure is centralized then we assign it zero value and if it is shared then we have given it one value. This variable has been supported by the study of Javid & Iqbal (2008).

VI. Firm's Performance

Firm's performance is one of the relevant constructs in the strategic management researches and in number of the researches it is frequently used as the dependent variable

3.5 Research Framework



3.6 Research Hypothesis

Suggested hypotheses are presented as followed:

Hypothesis 1:

Board size is positively associated with firm's performance.

Hypothesis 2:

Audit committee independence is positively associated with firm's performance.

Hypothesis 3:

CEO duality is positively associated with firm's performance.

Hypothesis 4:

Board independence is positively associated with firm's performance.

Hypothesis 5:

Ownership structure is positively associated with firm's performance.

4. Empirical Findings

Empirical findings and results are based on various statistical techniques. Before estimating the model, we computed the descriptive statistics of the variables. Later on, to determine the effect of various explanatory variables on performance of micro finance institutions working in Sialkot in context of corporate governance we computed multivariate regression.

4.1 Descriptive Statistics

The summary statistics of dependent and independent variables are illustrated in table 1.

Table 1: Descriptive Statistics of Variables

Variables	Mean	Standard Error	Standard Deviation
Performance of micro financial institution (PKR Millions)	41.7586	1.83202	9.86572
Board size (No.)	6.413	0.731	2.524
Audit committee independence (0=No,1=Yes)	0.447	0.483	0.118
CEO duality (0=No,1=Yes)	0.634	0.103	0.272
Board independence	0.467	0.683	0.138
Ownership Structure (0= centralized,1= share)	0.654	0.123	0.302

4.2 Multivariate Regression Analysis

OLS multivariate regression technique was employed to identify and analyze the impact of various corporate governance variables on the firm's performance because multivariate analysis depicts the cause and effect relationship among dependent and independent variables. The results of multivariate regression analysis are presented in table 2. We found that ownership structure and CEO duality are important factors in determining the performance of Micro-finance institutions. We found that on an average institution having shared ownership structure earn 16 percent more as compared to centrally controlled financial institutions. Similarly, if CEO duality exists then performance also improves. We also observed that on an average institution having CEO duality earn 52 percent more as compared to non-existence of CEO duality in the financial institutions. Furthermore, our results show that independent variables as board size, board independence and audit committee independence are non-significant in our research study.

Table 2: OLS Estimates of Multivariate Regression Analysis

Variables	Coefficients	SE	t-statistic	Sig.
Intercept	4.80	1.535	3.132	0.002*
Board Size	0.10	0.158	0.664	0.509 NS
Audit Committee Independence	0.19	0.190	1.029	0.307 NS
CEO Duality	0.52	0.158	3.301	0.001*
Board Independence	0.02	0.128	0.158	0.875NS
Ownership Structure	0.16	0.088	1.899	0.061**
R Square	0.398			
Adjusted R square	.158			
SE	1.654			
F value	28.18***			

Note: *=Significant at 5% level, **= Significant at 10% level, NS = Non-Significant

5. Discussion

In this study, we selected three microfinance institutions such as Tameer Microfinance Bank, Apna Microfinance Bank Ltd and Khushhali Microfinance Bank from Sialkot city itself. The main functions of the corporate governance must to assign these power decisions amongst those people who work for the development of microfinance institutions This study was conducted to delineate the impact of corporate governance (board-size, audit committee independence, CEO duality, board independence and ownership structure) on the performance of microfinancing institutions. As per findings of our research, the board size, CEO duality and ownership structure were influencing significantly on firm's performance and market value. These results have been supported by the research of Lensink *et al.*, 2018; Ault, 2016; Tiruneh, 2015. According to the results, it was analyzed that micro finance institutions of Sialkot, Pakistan should need to be improved in terms of top management, by giving independence to board size and audit committee etc. The recommendations are provided within the corporate governance and performance relationship in microfinance institutions to ensure improvement: Integration of advance information technology systems in existing business environment so that communication and collaboration network can be established in the micro finance institutions. The microfinancing organizations should be given special emphasis on these parameters for achieving their targets that will eventually contribute in the performance and market value of the organization.

6. Conclusion

Significance of corporate governance in any organization mainly microfinance institutions cannot be neglected at any instance, especially in the development, welfare, social justice, economic wellbeing to its employees. This research study was based on the top-level management such as board of directors, chief executive officers, managing directors and all the related staff who are responsible for the growth and progress of the microfinance institutions. The management of the microfinance institutions is divided into three major's components that are top level management, middle management and lower level management. Assessment mechanism needs to be improved so that better evaluation process can be integrated. Corporate governance bears substantial importance due to increasing demand for the transparency as well as accountability of funds and making good decisions that utilized and adopted in the microfinance activities and tasks. It is recommended that all the micro finance institutions should be registered under the State Bank of Pakistan authorized working in the country. It has been analyzed that there is a high probability that if the above recommendations are approached or considered the overall challenges indicated within the context of micro finance institution and corporate governance performance can be maximized for change.

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