

Effect of Corporate Governance on Corporate Performance: Sri Lankan Evidence

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Abstract

Effective corporate governance practices contribute significantly to various aspects of an organization as a strategic direction. This study examines the impact of corporate governance practices on corporate performance. The top fifty companies from five industries listed in the Colombo Stock Exchange were selected as the sample. Secondary data was extracted from financial statements covering a five year period from 2014 to 2019. Six corporate governance practices; financial acumen, board independence, board size, CEO duality, board committees, and board gender diversity were tested against corporate performance indicators: return on assets, return on equity, and Tobin's Q. Results of multivariate analysis indicated that board size and committees positively impact on corporate performance, while other variables do not provide any significance. The findings of the study will fill some gaps in extant literature in the corporate governance field. It may also facilitate significant policy implications relating to corporate governance by strengthening existing rules and regulations in the institutional framework.

Keywords-: Corporate Governance, Corporate Performance, Listed Companies

1. INTRODUCTION

Corporate governance is a mechanism that ensures that the management takes appropriate measures to safeguard the stakeholders' interests (Anandasayanan, 2018). Accordingly, corporate governance practices (CGPs) ensure the alignment of

objectives of the firm among the board of directors, shareholders, and other stakeholders when setting objectives, determining the ways of achieving them, and measuring performance. As a result of major corporate collapses that took place around the world, such as Enron,

WorldCom, and Sathyam, the extensive amount of regulatory consideration was focused on CGPs (Jackling & Johl, 2009). This would develop the quality and reliability of financial reporting and reduce the opportunistic behavior of the management (Niu, 2006). Simultaneously, corporate governance is a vital factor that drives the corporate performance of a firm. According to Pandey (2010), the ultimate objective of the entity is to maximize shareholder wealth by achieving the profits targets of the firm. By aligning the shareholders' interests with the management, corporate governance contributes to the success of an organization (Anandasayanan, 2018).

Firm performance is impacted by CGPs, as it influences the better management of the company (Heenetigala, 2011). Performance measures can be either qualitative or quantitative. These measures provide a tool for an organization to manage the progress toward the predetermined goal by defining key performance indicators. According to Guest et al. (2003), performance is a positive or negative outcome, results, and achievement of organizational activities. Further, they point out that there is a necessity to measure strategic practices in terms of outcome. These outcomes can

be identified as financial measures [e.g., Return on Assets (ROA), Return on Equity (ROE), Profit Before Tax (PBT), turnover], measures of production output (number of units produced, numbers of customers processed), measures of customer satisfaction (number of customer complaints) and measures of employee satisfaction (employee turnover). This study focuses on the corporate performance of the company.

In the Sri Lankan context, corporate governance came into the discussion table in 1997 with the introduction of a voluntary code for corporate governance. With the initiation of the Code of Best Practice on Corporate Governance 2008, which was introduced by the Institute of Chartered Accountants in Sri Lanka (ICSL) and Security and Exchange Commission (SEC), some principles of the voluntary code were incorporated into the listing rules (Section 7 of listing rules) as mandatory compliance for listed companies. Further, in 2017, ICSL and SEC issued a revised code of best practice by incorporating principles regarding cybersecurity and environment, society, and governance (ESG) reporting. However, past studies have come up with inconclusive findings in terms of the impact of CGPs on firm performance. CGPs within a firm provide an internal control framework

which consists of rules and practices in order to achieve firm's goals and objectives by minimizing various stakeholder conflicts. The effectiveness of these CGPs and internal control mechanisms depend on the attitude of higher-level management about CGPs. Internal control failures have caused a few well-known recent corporate collapses, such as Golden Key Credit Company, Pramuka Bank, and ETI Finance Limited. These corporate collapses direct to study how effective corporate governance practices in Sri Lanka. Lakshan and Wijekoon (2012) report that inconsistency in internal control procedures and CGPs indicate some failures in companies. Further, they highlight that poor CGPs enhance the probability of corporate letdown. Therefore, this study focuses on examining whether better CGPs in firms lead to better performance.

Many studies have identified agency theory as the cause of the emergence of corporate governance. According to Ross (1973), the lack of goal congruence between the board of directors and shareholders leads to the emergence of agency theory. Moreover, Arora and Sharma (2016) state that good CGPs improve the firm's performance by reducing agency costs. Effective corporate governance was highlighted through the recent corporate governance reforms in

order to protect the stakeholders' interests in the Sri Lankan context. Furthermore, Lakshan and Wijekoon (2012) state that though financial institutions are highly regulated, the collapse of some banks confirms the weaknesses of the governance system. Evidence of corporate scandals in history confirm that directors were alleged due to the lack of fiduciary duty toward the shareholders.

The adoption of CGPs has improved drastically in the business environment due to their increased importance. These practices have been recognized as a mandatory requirement to exist within the current business world. According to Wallington, Lawrence, and Loechel (2008), investors are willing to offer even a 25% premium to well-governed companies in Australia. Manawaduge (2012) pointed out that the Sri Lankan companies do not equally comply with the CGPs due to the difference in the companies' interests and the commitment to compliance. However, the importance of CGPs has not been undermined in any scenario. Accordingly, the current study aimed to examine the impact of corporate governance on the corporate performance of listed companies in Sri Lanka.

Though the researchers observed some evidence on the relationship between corporate governance and corporate performance in developed countries, the findings of those studies are less applicable to developing countries like Sri Lanka. This is primarily due to Sri Lanka's unpredictable economic situation, dynamic government policies, and unwanted political interferences. Therefore, it is worthwhile to study the relationship from the perspective of a developing country. Further, most of the prior studies focused on a few commonly used characteristics of corporate governance such as chief executive officer's (CEO) duality on firm's performance by narrowing down the scope of those studies (Velnamby, 2013). However, widening the scope this study investigated the impact of rarely used variables, particularly financial acumen and gender diversity along with commonly used four variables. Furthermore, this study's outcomes encourage companies to implement good CGPs constantly to improve their performance. The study's findings and recommendations will assist regulators and policymakers in Sri Lanka, such as the ICSL and the SEC, in enhancing the grey areas of corporate governance regulations. Furthermore, because corporate governance is

so crucial to an organization's existence, this research gives the business information into how to improve its CGPs.

Hence, the current study would contribute to the existing literature and fill the gaps prevailing in the existing literature.

2. LITERATURE REVIEW

2.1 Corporate governance

Better governance mechanism has become one of the imperative causes of success in many organizations and the economy of a country at last. It has become a tool for enhancing the triple bottom line (profit, people, and plant) of the firm (Sarah, 2017). Good CGPs assist a firm for sustainable economic development by improving the corporate performance of the firm. According to Rajendran (2012), in the 1980s, the word corporate governance came into the discussion as a crucial theme. Further, he identified corporate governance as a mechanism of building the relationship between a firm's management and its stakeholders such as shareholders, lenders, regulators and the general public. As per Laporta, Lopez and Sheleifer (1998), the macroeconomic factors within which a firm operates strongly affect the corporate governance of the

country. The implementation of CGPs not only enhances the profitability of the firm but also improves the level of public confidence (Anandasayanan, 2018). Thus, the board of directors has great pressure to implement CGPs to ensure enhanced profitability and serve the interest of stakeholders (Abor & Biekpe, 2007). Bhatt and Bhatt (2017) stated that CGPs vary from country to country based on the institutional development background. Further, Adegbite (2012) remarked that the corporate governance model and regulations are affected by the country's institutional arrangements. These institutions are regarded as fundamental and inseparable components of any country and facilitate the accomplishment or failure of good corporate governance.

As stated by Azeez (2015), the ICSL introduced the first voluntary code in 1997. Further in 2008, 2013 respectively ICSL issued code of best practice cooperatively with the SEC. The revised code of best practice was recently issued in 2017 by ICSL and SEC incorporating the principles regarding cybersecurity and environmental, social and governance (ESG) reporting. The development of corporate governance codes in Sri Lanka has mainly happened with the development of UK corporate

governance codes (Senaratne, 2008).

As discussed above, many researchers had spent considerable effort in studying CGPs. Ehikioya (2009) used CEO duality, ownership concentration, directors' shareholding, board skill and board member relative on the board to measure CGPs. Board size, board independence, audit committee independency, incentives and meetings, and financial expert have been used to measure corporate governance by Farhan, Obaid, and Azlan (2017). Accordingly, various researchers have used different kind of variables in their research studies. However, it is hard to use all of those variables in a single study due to time constraints. As a result of a thorough review of previous literature and discussions on each variable, six variables were chosen for the current research and are described in the following sections.

2.1.1 Financial acumen

As per the fourth principle of the code of best practices on corporate governance 2017, the board should have financial acumen in order to provide insights into financials to the board. The financial expertise on the board increases the effectiveness of decision-making by incorporating

financial insights into the decision (Krishnan & Lee, 2009). Further, the financial experts on the board should have capabilities to oversee the possible failures in financial reporting and litigation matters of regulators (García-Sánchez, Martínez-Ferrer, & García-Meca, 2017).

2.1.2 Board independence

Board independence is a major characteristic of an effective board. Jensen and Mackling (1976) argued that the board which comprises a higher number of non-executive directors improves the firm performance by enhancing monitoring and controlling functions. Further, Jensen and Mackling (1976) emphasized the representation of non-executive directors on the board reduces the opportunistic behavior of executive directors. Dahya and McConnel (2007) investigated that firm's performance can be increased through incorporating non-executive directors in UK firms. The effectiveness of non-executive directors affects their relationship with the executive directors and the tenure (O'Sullivan & Wong, 1999). In contrast, due to non-executive directors' part-time involvement and lack of time for the firm activities may lead to a reduced contribution of non-executive directors to the firm

performance (Weir, Laing, & McKnight, 2002).

2.1.3 Board size

The number of directors within the board can be identified as board size. Since the larger board has a negative impact on firm performance, a reasonable size of the board is recommended by many academics (García-Ramos & García-Olalla, 2011). This is mainly due to the increment in cost with larger boards and the delay in the decision-making process with the communication issues. On the other hand, some scholars preferred a larger board, as it provides better insights and resources for decision making and pool of experience. As per Abor and Biekpe (2007), board size has a positive impact on the profitability of the companies in Ghana. Oppose to the above findings, Ujunwa (2012) established a negative impact of board size on the corporate performance. He suggested that the board size has a negative impact on corporate performance due to an increase in free riders in the board, leading to a reduction in efficiency in monitoring the management. On the other hand, small size of boards is encouraged due to the provision of better quality information to the investor with a higher level of accountability (Bushman, Piotroski, & Smith, 2004).

2.1.4 CEO duality

CEO duality indicates the structure of the board showing whether there is a separation of roles between CEO and chairman. As per Lam and Lee (2008), a combination of two roles leads to the creations of a powerful CEO which results in ineffective performance. In contrast, Fama and Jenson (1983) emphasized that the separation of CEO and chairman is vital in order to solve the agency problem by safeguarding the interests of shareholders.

Moreover, Ujunwa (2012) suggested that CEO duality negatively affects the corporate performance of Nigerian companies. The separation of CEO and chairman increases the cost of the firm with the disruption of information flow between two roles which may lead to an increase in the cost of the firm (Vafeas & Theodorou, 1998).

2.1.5 Board committees

Board committees play an important role in eliminating agency conflict between management and shareholder (Rezaee, 2009). As per the code of best practice on corporate governance (2017), audit committee, remuneration committee, and nomination committee are recommended to establish within the firm. These committees need to be independent and competent in

order to perform the assigned duties (Keogn, 2002). Davis (2002) emphasized that when there is a board committee with separate key responsibilities, stakeholders' confidence in the corporate board is enhanced. In contrast, there was also evidence to support the view that board subcommittees had no effect on firm performance (Vafeas & Theodorou, 1998). As per the findings of Weir, Laing and McKnight (2002), board sub-committees have no relationship with the performance but there is a weak association with the committee director quality and the performance.

2.1.6 Gender diversity

Gender diversity is a part of board diversity (Milliken & Martin, 1996), which affects the effectiveness of the board as per the code of best practice on corporate governance. Hanson and Mullis (1985) stated that women are clever at building a relationship between management and shareholders. Further, women's participation in the board improves the transparency of board activities. Bianco, Ciavarella and Signoretti (2015) argued that female participation on corporate boards improves the firm corporate performance. In contrast, Ujunwa (2012) reported a negative relation between femininity diversity and corporate performance due

to the delay in decision making which negatively affects the performance of the firm. However, some other researchers (Rose, 2007; Marimuthu & Kolandaisamy (2009) have been unable to report a relationship between gender diversity and corporate performance. Hence, the findings are inconclusive.

2.2 Corporate Performance

Corporate performance as an indicator of a firm's operational efficiency has much more interested among many researchers. Accounting ratios, market ratios, and a mix of both accounting and market ratios have been used by many scholars throughout their studies to measure corporate performance (Kiel & Nicholson, 2003). The most commonly used accounting ratios are ROA, ROE, and Earning per Share (EPS) (Baysinger & Butler, 1985). Tobin's Q is the most commonly used market-based performance measurement. Bhunia, Mukhuti, and Roy (2011) suggested that the corporate performance of the firm indicates the financial healthiness of the relevant firm. As Halimatusadiah, Sofoanty and Ermaya (2015) suggest, the corporate performance of a firm is mainly indicated through the level of firm's profitability. The overall success of the firm and level of achievement of objectives are fundamentally

measured using the profitability of the firm in a particular accounting period. Further, the generation of net income consistently indicates the better corporate performance of the firm.

On the other hand, there are several limitations of the accounting-based measures against market-based measures. The accounting-based measurements can be simply manipulated by the management through accounting practices. But, the market-based measurements are distorted from management. Hence, the possibility of manipulation is limited.

According to Velnampy and Niresh (2012), ratios are mostly used in evaluating the corporate performance of the firm because a large quantity of data can be summarized by using ratios. Therefore, the corporate performance of the firm can be measured using several ratios such as profit margin, ROA, ROE, EPS, and Return on Investment (ROI) (Halimatusadiah et al., 2015). Research conducted by Velnampy (2013) used ROA and ROE as the measure of firm performance. Anandasaynan (2018) used ROA as a performance indicator in the study, which was carried out in the Sri Lankan context. Thus, a mix of accounting-based and market-based ratios has been

used to measure the firm's performance in this study.

2.3 Corporate Governance and Corporate performance

A considerable amount of researches on the theme have been conducted by many scholars across the globe. However, several inconclusive findings have been identified, such as positive, negative, and insignificant relationships in the local and international context, as described below.

2.3.1 Local context

As per Anandasayanan (2018), an important role is played by the corporate governance mechanisms on the corporate performance of diversified holding companies in Sri Lanka. This is because a large board of directors may improve the profitability of diversified holding companies. Profitability is improved by the board composition.

Further, Anandasayanan (2018) stated that the application of good CGPs helps the organization to achieve its objectives and raise profitability. Similarly, a positive association is identified between CEO duality and firm performance by Azeez (2015). This means that the separation of two designations of CEO and chairman improves the firm's performance due to the separation of unfettered power between two individuals. The

study of CGPs relating to banks conducted by Rajendran (2012) found a positive association between board committees (audit, remuneration, and nomination) and firm's performance. Moreover, firm's performance is positively associated with variables such as board meetings, board size, and non-executive directors. But, this study suggested that a board should be comprised of 50% of non-executive directors though the code indicates two-third. Wijethilake, Ekanayake and Perera (2015) concluded, frequency of board meetings, shareholding of board members, CEO duality and board committees have a positive impact on firm performance.

According to the results of the study done by Azeez (2015) about corporate governance and firm performance in Sri Lanka, board size is negatively related to firm performance. This indicated that minor boards with a small number of members improve the performance due to the possibility of close monitoring and supervision. Rajendran (2012) highlighted the separation of leadership structure is negatively related to the firm performance of the banking sector. Further, Wijethilake et al. (2015) argued size of the corporate board has a negative impact on firm performance.

2.3.2 International Context

Abor and Biekpe (2007) found a significant positive association between board size and performance and a relatively large board of directors is better as it has broad expertise for better decision making. Further, this study suggested that firm profitability is positively influenced by board composition. There is a significant positive relationship between CEO duality and firm performance. The higher percentage of foreign ownership improves profitability. Bhatt and Bhatt (2017) remarked that the profitability of the firm is improved by the implementation of a better governance system. The existence of a robust corporate governance code by the government is a vital factor in enhancing CGPs. Halimatusadiah et al. (2015) reported that implementation of better CGPs improves the ROA in the Indonesian context. Further, they pointed out this may be due to the greater public confidence and continuous implementation, and development of good CGPs.

Berthelot, Francoeur, and Labelle (2012) revealed that the percentage of independent directors, usage of stock options, and frequency of board meetings are significantly and negatively related to the net income of Canadian firms.

Furthermore, Paniagua, Rivelles, and Sapena (2018) also revealed an opposite relationship between the number of board members and ROE. According to them, if there are more directors, it implies a higher payment for them and results in a lower ROE. According to Jadiyahappa, Jyothi, Sireesha, and Hickman (2017), female CEOs negatively impacted Indian firms' performance. As per the researchers, this is mainly due to the social status of females in India.

According to Arora and Sharma (2016), the association between corporate governance and firm performance was not strong as firms are not following the rule and regulations on corporate governance strictly in the Indian context.

When reviewing existing literature, it seems that a dearth of studies has been performed by examining the relationship between corporate governance and corporate performance after 2017 with the introduction of the *Revised Code of Best Practice* in Sri Lankan Context. The large corporate collapses during the last decade such as Golden Key Credit Company and ETI Finance Limited, question the existing corporate governance practice prevailing in the Sri Lankan context. Further, the macro factors have

been drastically changed in the last few years due to the current economic and political conditions in Sri Lanka. In order to pass through these conditions, there is a necessity for good CGPs in an organization. Further, the corporate governance variables such as female directors which imply gender diversity in the board, and financial acumen which is a principle in corporate governance code in Sri Lanka are not much researched in the Sri Lankan context. Therefore, this study is planned to contribute to existing literature by adding more corporate governance variables.

3. METHODS

Conceptual framework developed based on the existing literature depicted in figure 1.

All companies listed in the CSE were considered as the study's population, where a sample of 50 companies was drawn from 5 industries; Food, beverage and tobacco, consumer services, capital goods, materials, and real estate for the present study. These 50 companies contained 10 companies from each selected industry sector. The selection of five industries was based on the highest number of companies available in the industries and a sample of 50 companies was based on the highest turnover of the selected

industry. Accordingly, the sampling procedure used for the study was the convenience sampling method.

3.1 Data Collection

Data collection was mainly based on the secondary data. Published annual reports of sample companies for the period between 2014/2015 and 2018/2019 were used.

3.2 Method of Data Analysis

This study adopted the quantitative research approach. Accordingly, gathered data from the annual reports of public listed companies were analyzed using STATA statistical software. Descriptive, correlation, and panel regression analysis were employed as the data analyses techniques of this study.

The following regression models were used to assess the impact of corporate governance on firm corporate performance. As per Table 2, firm size and leverage were used as control variables. Regression equations are as follows:

$$\text{Corporate performance}_{ROE} = \beta_0 + \beta_1 FA_{it} + \beta_2 BI_{it} + \beta_3 BS_{it} + \beta_4 CEO_{it} + \beta_5 BC_{it} + \beta_6 GD_{it} + \beta_7 FSIZE_{it} + \beta_8 LEV_{it} + \varepsilon \dots \dots \dots (1)$$

$$\text{Corporate performance}_{TBO} = \beta_0 + \beta_1 FA_{it} + \beta_2 BI_{it} + \beta_3 BS_{it} + \beta_4 CEO_{it} + \beta_5 BC_{it} + \beta_6 GD_{it} + \beta_7 FSIZE_{it} + \beta_8 LEV_{it} + \varepsilon \dots \dots \dots (2)$$

$$\text{Corporate performance } ROA = \beta_0 + \beta_1 FA_{it} + \beta_2 BI_{it} + \beta_3 BS_{it} + \beta_4 CEO_{it} + \beta_5 BC_{it} + \beta_6 GD_{it} + \beta_7 FSIZE_{it} + \beta_8 LEV_{it} + \varepsilon \dots \dots \dots (3)$$

4. RESULTS

4.1 Descriptive Analysis

Availability of financial acumen has the mean of 1.00 with the standard deviation of 0 which indicates all the companies consists of a board that has financial expert in order to provide necessary consultation to the board. Board independence which is the proportion of non-executive directors on the board ranges from 25% to 100% by showing a mean of 69%. CEO duality which shows the separation of chairman and CEO has a mean of 0.86 with the variation of 34%. Audit, remuneration, and nomination committees were considered as board committees in the study. Fourty five percent of the sample has all three committees. Gender diversity indicated the proportion of female directors in the board which has quite a low mean of 11%. Board size is measured using natural logarithm of number of members in the board which has mean of 2.055 and it approximates the maximum value of the board size.

ROE, ROA, and Tobin's Q have been used to measure the firm corporate performance. ROA is

5% in an average firm with a deviation of 6.3%. ROE is 6% in an average firm ROE held by the companies with a variation of 9.7%. When considering the Tobin's Q, a large variation can be observed in the selected sample of companies due to the higher standard deviation of 0.66.

It is important to understand the descriptive nature of control variables as they cause an impact in measuring the relationships among the core variables. The variable firm size takes the highest mean value out of the two control variables while it is also subjected to the highest variation where the minimum and maximum figures vary from 20.18 to 24.25. The mean and standard deviation respectively for leverage is 0.32 and 0.23, indicating that companies have low levels of debt compared to their total assets, with a 23% deviation.

4.2 Correlation Analysis

A correlation coefficient is a statistical measure that measures the degree to which changes of one variable predict the changes of the other variable. Pearson correlation analysis was performed to identify the relationships between independent, dependent, and control variables.

As per Table 3, results of correlation, financial acumen has a significant weak negative relationship with Tobin's Q ($p < 0.05$) while it shows no significant relationship with ROE and ROA. There is a significant weak negative relationship between Board independence and Tobin's Q and it does not have a significant relationship with ROE and ROA. Further Board size shows a significant weak positive relationship between ROE, Tobin's Q, and ROA. CEO duality and gender diversity does not depict a significant relationship between any dependent variable. Board committee's variable has significant weak positive relationship between ROA, ROE, and Tobin's Q.

Further when considering the relationship between dependent variables ROA, ROE and Tobin's Q with control variables, ROA and ROE show a significant weak positive relationship with firm size. However, Tobin's Q shows a significant weak positive relationship only with leverage.

4.3 Multivariate Analysis

In order to identify the impact between CGPs and corporate performance, the panel regression was carried out on the three dependent variables. Cross-sections among the

observation have been considered. Therefore, it provides an opportunity to identify whether an impact is coming to the measured the relationship between corporate governance and corporate performance from cross-section; firms' values for five years. Hausman test was performed to select the most appropriate model among Fixed and Random Effect models. Table 4 provides the findings which arrived from the Hausman test.

Since the significance value is less than 5% for Tobin's Q, it is believed that Fixed Effect Model would be the most appropriate model in performing the panel regression for Tobin's Q. Since the significance value is greater than 5% for ROE and ROA, Random Effect Model is most appropriate for panel regression analysis of ROE and ROA. Panel regression analysis (Table 4) shows the derived results from the Fixed Effect Model and Random Effect Model.

The R squared (R^2) value measures the percentage of the variance in the dependent variable that is explainable from the independent variable. As per the observation of model 1, 9% of the ROE is explained by independent variables. Similarly, 16% of Tobin's Q (model 2) and 11% of ROA

(model 3) are explained by the independent variables used in the study. The panel regression result for ROE shows that the independent variables do not have a significant association with ROE except for board committees and board size which showed a positive relationship with ROE. The results for Tobin's Q show that board independence has a significant negative relationship and board size has a significant positive relationship. Other independent variables do not depict a significant relationship with Tobin's Q. The results of panel regression analysis for ROA show that Board size has a significant positive relationship with ROA while other independent variables do not show any significant association with ROA.

5. DISCUSSION

The level of CGPs in the Sri Lankan context was measured using descriptive statistics. As per the findings of the study, it was able to identify that the financial acumen represented a compliance mean of 100%, board independence showed a mean of 69%, CEO duality depicted a mean of 86%, board committees showed a mean of 45% while gender diversity represented a mean of 11%. Other than gender diversity, all other variables showed

significant compliance with the corporate practices in Sri Lanka.

The relationship between CGPs and firm corporate performance was examined using correlation analysis and panel regression analysis. Correlation analysis and the panel regression analysis indicate a significant weak positive relationship between board size, board committees, and corporate performance which was measured through ROE, Tobin's Q, and ROA. However, it should be noted that, since all analyses did not provide consistent results on the association of corporate governance characteristics with corporate performance, it was concluded that there is mixed evidence on the impact on the selected corporate governance characteristics and firm corporate performance.

The result related to the financial acumen in all three models indicated an insignificant impact. Thus, the financial acumen has no impact on corporate performance in the selected companies. Guner, Malmendier, and Tate (2006) suggested that, in the absence of conflict of interest, there is no significant impact of financial experts on firm performance. In contrast to the finding of this study, the financial expertise on the board increases the effectiveness of decision-making by inserting the

financial insights into the decision-making (Krishnan & Lee, 2009).

The results related to board independence in all three models indicated an insignificant impact. Thus, board independence has no impact on corporate performance. This is similar to some prior scholars' findings. As per Azeez (2015), the presence of non-executive directors on the board are not associated with firm performance of the listed companies in Sri Lanka. But, Jensen and Mackling (1976) emphasize the representation of non-executive directors on the board reduces the opportunistic behavior of executive directors. Fama and Jensen (1983) highlight the importance of having non-executive directors on the board in terms of expertise and connections which will ultimately enhance firm performance.

Board size has a significant impact on corporate performance as per the results of all three models. Thus, board size has a positive impact on corporate performance. As per prior findings, reasonable board size affects firm performance in effective controlling (García-Ramos & García-Olalla, 2011). Board size enhances the firm performance by adding more experience to the board (Haniffa & Hudaib, 2006). But the results

of the study contrast with the findings of both Velnampy (2013) and Azeez (2015).

CEO duality shows no significant impact on the corporate performance as per the results of all three models. These results are similar to a prior study carried out by Rajendran (2012) which indicates the separate leadership structure has no significant impact on the corporate performance. In contrast, Fama and Jensen (1983) emphasized that the separation of CEO and chairman is vital in order to solve the agency problem by safeguarding the interests of shareholders.

The results related to board committees have indicated a significant impact in model 1. Therefore, board committees have a positive impact on ROE. Laing and weir (1999) also identified that corporates with board committees have a significant positive impact on firm performance since investors consider the existence of board committees when making investment decisions. But, as per the results of the studies carried out by Velnampy (2013) and Rajendran (2012), board committees have no impact on corporate performance.

Gender diversity has no impact on corporate performance. This result was confirmed by

Jadiyappa et al. (2017) by stating gender diversity has no significant impact on firm performance. In contrast, as per Bianco et al. (2015), female participation on corporate boards improves the firm corporate performance.

6. CONCLUSION

The empirical findings of the current study extended the understanding of CGPs in Sri Lanka and its impact on corporate performance. As per the findings of the current study, board size has significant positive relationship with corporate performance. Board committees has a positive impact on corporate performance as per the current study.

Based on the findings of the current study, since the board size has a positive impact on the corporate performance, it is recommended companies to maintain a well-balanced effective board. Such a board provides the necessary guidance and oversight to the companies in order to achieve the goals and objectives of the firm.

Board committees of a firm have an impact on corporate performance. The board committees should accountable to the shareholders of the firm in order to protect the interest of shareholders. Further,

strengthening board committees resolves the agency problem by providing necessary oversights to the board of directors. Hence, the board committee structures which were adopted by the companies with the recommendation of code of best practice should be strengthened within the CGPs in Sri Lanka. Further, it is encouraged to adopt these practices since it improves investor relations and improves the market performance of the company.

New insights of the study may benefit interested parties in Sri Lanka such as shareholders, regulators, boards of corporations. Moreover, the findings of this study will assist policymakers in promoting the progression of corporate governance mechanisms in Sri Lanka. Policymakers could take indispensable actions to promote CGPs. Using a sample of Sri Lankan listed companies over the period 2014-2019, this study has contributed to the literature by assessing the impact of corporate governance in the Sri Lankan context on corporate performance. Further, the study does not find conclusive evidence on the anticipated positive association between CGPs and performance in the Sri Lankan context. Hence, policymakers are requisite to scrutinize the reasons for such absence and strengthen the postulated rules, regulations, and laws on CGPs.

APPENDIX

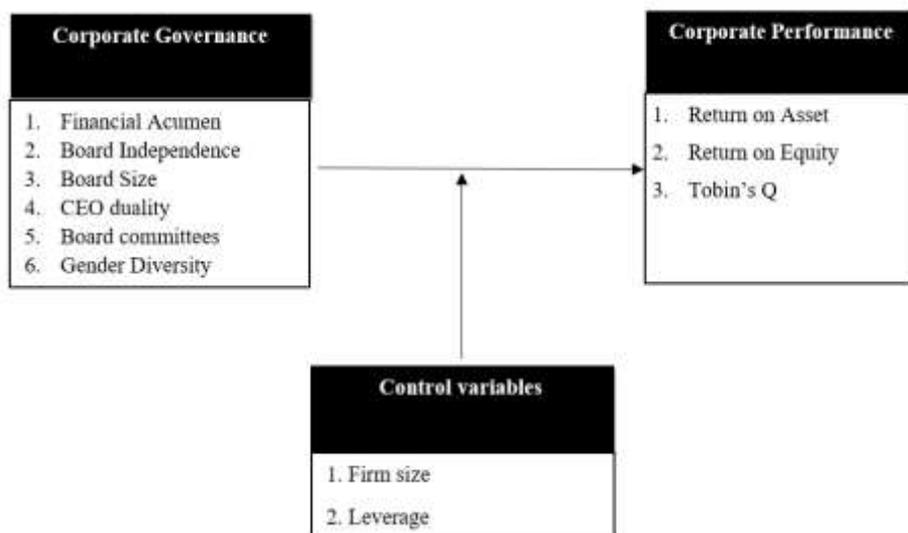


Figure 1: Conceptual Framework

Table 1: Operationalization of Variables

Variable	Measurement	Literature
<i>Dependent Variables</i>		
ROA	Earning before interest and Tax / Total assets	Anandasayanan (2018), Arora and Sharma (2016)
ROE	Net income / Total equity	Anandasayanan (2018), Valenti, Luce and Mayfeild (2011)
Tobin's Q	(Market value of equity+ Book value of liabilities)/ Total assets	Farhan et al. (2017), Ehikioya (2009)
<i>Independent Variables</i>		
Financial Acumen (FA)	A dummy variable equals 1 if the board has financial experts and otherwise 0	McIntyre, Murphy and Mitchell (2007)
Board Independence (BI)	Proportion of number of non-executive directors to the total number of directors on the board	Arora and Sharma (2016), Dharmadasa, Gamage and Herath (2014), Wang and Oliver (2009)

Board Size (BS)	Natural logarithm of number members on the board	Anandasayanan (2018), Farhan et al. (2017), Ehikiyoa (2009)
CEO Duality (CEOD)	A dummy variable equals 1 if the CEO duality exists and otherwise 0	Mishra and Mohanty (2014)
Board Committee (BC)	Dummy variable equals 1 if all three committees are present and otherwise 0	Heenetigala (2011), Weir et al. (2002)
Gender Diversity (GD)	Percentage of female directors on the board	Benedicto, (2015), Dharmadas et al. (2014)
Control Variables		
Firm Size (FS)	Natural logarithm of total assets	Arora and Sharma (2016), Wang and Oliver (2009)
Leverage (Lev)	Total debt/ Total assets	Farhan et al. (2017), Wang and Oliver (2009)

Table 2: Descriptive Statistics

Variable*	Mean	SD	Minimum	Maximum	Skewness	Kurtosis
FA	1.0000	0.0000	1.0000	1.0000	-6.2582	37.4605
BI	0.6936	0.1917	0.2500	1.0000	-0.0494	-0.8769
BS	2.0550	0.2733	1.1000	2.5600	-0.7465	0.3640
CEOD	0.8600	0.3487	0.0000	1.0000	-2.0887	2.3779
BC	0.4520	0.4987	0.0000	1.0000	0.1948	-1.9788
GD	0.1131	0.1159	0.0000	0.5600	1.1836	2.3517
ROE	0.0613	0.0979	-0.1700	0.2300	-14.8398	22.5835
Tobin's Q	0.9842	0.6657	0.2500	2.8100	3.7999	21.0717
ROA	0.0569	0.0634	-0.0600	0.1800	-1.1900	10.2795
FSIZE (Ln)	22.3249	1.1968	20.1800	24.2500	0.1440	-0.7372
LEV	0.3243	0.2300	0.0200	0.7800	0.5156	-0.6061

Notes: Due to the presence of significant outliers, winsorized version of 5% for ROE, ROA, Tobin's Q, FSIZE and LEV variables have been considered for descriptive analysis and other analyses depicted in correlation analysis and panel regression.

Source: Analysis Results (2020)

Table 3: Correlation Matrix

Variables	FA	BI	BS	CEOD	BC	GD	ROE	TBQ	ROA	FSIZE	LEV
FA	1.0000										
BI	0.1304*	1.0000									
BS	-0.0569	-0.1581*	1.0000								
CEOD	-0.0256	0.1286*	0.0590	1.0000							
BC	-0.0698	0.0365	0.1991*	0.1348*	1.0000						
GD	0.0072	-0.2696*	0.0382	0.0986	-0.0530	1.0000					
ROE	-0.0510	-0.0875	0.1792*	-0.1032	0.0637	-0.0179	1.0000				
Tobin's Q	-0.1427*	-0.2270*	0.2604*	0.0560	0.1281*	-0.0575	0.3789*	1.0000			
ROA	-0.0731	-0.0653	0.2195*	-0.0376	0.1337*	0.0380	0.8891*	0.3522*	1.0000		
FSIZE	-0.0348	-0.1055	0.2181*	-0.3161*	0.2113*	-0.0343	0.2428*	0.1171	0.2906*	1.0000	
LEV	0.0757	-0.0884	0.2238*	0.0011	0.1702*	-0.2059*	-0.0168	0.2407*	0.0436	0.1587*	1.0000

Notes: N = 250, *, ** significant at 0.05 and 0.01 levels (two-tailed), respectively

Source: Analysis Results (2020)

Table 4: Panel Regression Analysis

Variables	Dependent Variable: ROE Model I (Random)		Dependent Variable: Tobin's Q Model II (Fixed)		Dependent Variable: ROA Model III (Random)	
	Coef.	Std. Err.	Coef.	Std. Err.	Coef.	Std. Err.
FA	-0.0318	0.0973	-0.9507	0.6291	-0.0486	0.0619
BI	-0.0291	0.0342	-0.6735	0.2208	-0.0029	0.0218
BS	0.0531*	0.0236	0.3690*	0.1527	0.0356*	0.0151
CEOD	-0.0115	0.0191	0.1803	0.1224	0.0044	0.0121
BC	0.0021*	0.0129	0.0994	0.0840	0.0062	0.0082
GD	-0.0402	0.0564	-0.3834	0.3640	0.0184	0.0359
FSIZE	0.0166*	0.0056	0.0333	0.0368	0.0136*	0.0036
LEV	-0.0414	0.0283	0.5095*	0.1822	-0.0082	0.0180
Constant	-0.3427	0.1663	0.5587	1.0759	-0.2781	0.1059
R²	0.0890		0.1623		0.1183	
Sig. Value	0.0027		0.0310		0.0001	
Hausman test Chi (z²) Prob. Coef.	2.22 0.9736		16.76 0.0327		2.42 0.9651	

Notes: N = 250, *, **significant at 0.05 level, 0.01 (two-tailed).

Source: Analysis Results (2020)

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