International Journal of Business and Management Invention
ISSN (Online): 2319 – 8028, ISSN (Print): 2319 – 801X
www.ijbmi.org Volume 2 Issue 9‖ September. 2013‖ PP.01-06

Relationship Between Corporate Governance And Organizational Performance: Nigerian Listed Organizations Experience.

[1,]Adebayo O. S , [2,]Ayeni Gabriel Olusola[3,]Oyewole Felicia Abiodun
[1,]Department Of Management And Accounting
Ladoke Akintola University Of Technology, Ogbomoso, Nigeria
[2,]Public Administration Department The Polytechnic, Ibadan, Nigeria
[3],Purchasing And Supply Department Osun State Polytechnic, Iree, Nigeria

ABSTRACT :*This study examined the relationship between three corporate governance mechanisms (Board independence, board size, and chief executive duality) and two organization performance measures (earnings per share and return to equity) of Nigerian listed organizations.The data used for this study were derived from the audited finance statements of the firms listed on the Nigerian Stock Exchange (NSE) between 2005 – 2010 which comprises of fifteen (15) manufacturing firms and fifteen (15) financial and service institutions respectively as sample size. Panel data methodology was adopted because it combined time series and cross sectional data. The method of analysis is that of multiple regressions and the method of estimation is Ordinary Least Squares (OLS). The result showed that there is positive significant relationship between board independence and organizational performance while board size and chief executive duality have negative significant relationship with organizational performance. It is recommended that the office of chairman and chief executive officer should be occupied by different person in order to enhance check and balance also Small size boards and board independence should be put in place.*

Key words: *Corporate governance, Board, Shareholders, Earning per share and Return on equity.*

I. INTRODUCTION

Corporate governance has been considered as one of the most critical factors influencing firm performance. Corporate governance is concerned with ways in which all parties (the stakeholders) interested in the well-being of the firm attempt to ensure that managers and other insiders are always taking appropriate measures or adopt mechanisms that safeguard the interests of the stakeholders. Such measures are necessitated because of the separation of ownership from management, an increasingly vital feature of the modern corporations (Waseem, Saleh and Fares, 2011).

Magdi and Nadereh (2002) stressed that corporate governance is about ensuring that the business is runwell and investors receive a fair return. Shleifer and Vishny (1997)defined corporate governance by stating that it deals with the ways in which suppliers of finance to corporations assure themselves of getting a return on their investment. Corporate governance specifies the distribution of rights and responsibilities among different participants in the corporation such as, the board, managers, shareholders and other stakeholders, and spells out the rules and procedures for making decisions on corporate affairs. By doing this, it also provides the structure through which the company's objectives are set and the means of attaining those objectives and monitoring performance (Kajola, 2008).Corporate governance tools assure shareholders of adequate returns on investments. Waseem, Saleh and Fares, (2011) agreed that when these tools are not exiting or did not function properly, outside investors would neither invest in company equity securities nor lend to company. And this may cause company not to have access to long term debts andtherefore the overall economic performance would suffer because many good business opportunities would be missed and financial distress at individual firms would spread quickly to other firms, employees, and consumers.In the case of Nigeria, tribalism, inexperience directors, unqualified staff, poor management, lack of standard practice, inadequate polices and weak internal control systems account for some of the lapses in the operation of some corporate organizations. And that is why many organizations in Nigeria were distressed especially most public corporations and private companies, such as NITEL, NEPA, NRC, Machine Tools, Steel Rolling,

Nigerian Tobacco Company, Exide Battery, Leventis, National Banks, Forum Finance Limited, Global Bank, etc. It is on this note that this study wishes to examine the impact of corporate governance on organizational performance.

II. REVIEW OF LITERATURE AND HYPOTHESIS DEVELOPMENT

Previous research (Kajola, 2008; Waseem, Saleh and Fares, 2011; Abdullah, 2004; Coskan, and Sayiar, 2012; Fauziah, Yusoff and Adamu, 2012; Shukeri et al., 2012) discovered a number of corporate governance components have influence on firm performance, such as number or percentage of independent directors, board leadership structure, board size, board attributes, audit committee, and board meeting. It is acknowledged that there is no single characteristic that explain general pattern of links between corporate governance and firm performance. The relationship between corporate governance and firm performance is more "varied and complex" than can be covered by any single governance theory (Fauziah, Yusoff and Adamu, 2012). For the purpose of this paper, only three corporate governance components are found to be the most important determinant of financial performance are reviewed. They are number of independent director on the board; board leadership structure; and board size.

2.1 INDEPENDENT DIRECTOR ON THE BOARD

From the agency theory perspective, independent directors contribute toeffective governance by exercising control over top managers' decision-making, because theyare seen as the check and balance mechanism to enhance board's effectiveness. Board independence is considered crucial because outside directors are considered astrue monitors' and can discipline the management and improve firm performance (Duchin et al., 2010). Outside directors being financially independent of management, free from potentially conflicting situations are able to alleviate agency problems and curb managerial self-interest (Rhodes et al., 2000). They can protect the shareholder interest, perform monitoring and control function in a better way to align firm resources for better performance (Naveen and Singh, 2012). Previous empirical studies on the relationship between effectiveness outside director and organization performance are mixed. Some researchers (Awan, 2012; Choi et al, 2007;Abor and Adjasi, 2007; Xie et al., 2003 and Naveen and Singh, 2012)found a positive effect on the firm performance as a result of having independent directors on the company board.While some researchers (Kajola, 2012; Zong-Jim and Xiao-Lan, 2006) discovered that there is no any relationship between board composition with representation of outside independent directors and firm performance. It was argued that independent directors were not selected based on their expertise and experience, but more often for political reasons to legitimate business activities and for contacts and contracts. Due to lack of expertise, lack of required skills and knowledge of company affairs, such directors would not be able to perform their roles effectively (Rahman and Mohamed Ali, 2006).Therefore, it is hypothesized that:

Hypothesis 1. There is no significant relationship between board independence and firm performance.

2.2 CHIEF EXECUTIVE OFFICER STATUS

Agency theory argued for a clear separation of the responsibilities of the CEO and the chairman of the board and seems to prefer to have separate leadership structure. Coskan and Sayiar, (2012) argued that if the CEO and the chairman of the board is the same person, there would be no other individual to monitor his or her actions, and CEO will be very powerful and may maximize his or her own interests at the expense of the shareholders. Several empirical studies on the relationship between CEO duality and firm performance are mixed. Some authors (Kajola,2012 ;Yermack, 1996; Schmid and Zimmermann, 2005; Elsayed, 2007 and Abdullah, 2006) found that CEO duality had no impact on corporate performance. They argued that firms that had duality roles were not performing as well as their counterparts with separate board leadership. They also asserted that firmsare more valuable when the CEO and the chairman of the board positions are occupied by different persons. In the contrary, Tin Yan and ShuKan, (2008); Joshua, (2007) and Harjoto and Hoje, (2008) found a positive relationship between CEO duality and firm values and performance. They believed that the duality role is more effective, because one individual can exercise full control over the firm and the person can provide a centralized focus on achieving organizational goals.
Therefore, it is hypothesized that:

Hypothesis 2. There is no significant relationship between CEO-duality and firm performance.

2,3 Board Size.

Board size refers to the number of directors sitting on the board. Kajola, (2012) believed that limited board size to a particular level will improve the performance of a firm because the benefits by larger boards of increased monitoring are outweighed by the poorercommunication and decision making of larger groups. The impact of board size on board and firm performance has been a matter of continuing debate. Dey and Chauhan (2009) revealed that, as board size increases, group dynamics, communication gaps, and coordination cost increase. Sanda*et al* (2003) also reported that firm performance is positively correlated with small as opposed to large boards. Mark and Kusnadi (2005) agreed that a small size board has positive relationship with high firm performance. However, Andres and Vallelado (2008) and Chen et al. (2006) revealed larger boards are more efficient in monitoring and advising functions and create more value for a firm. Therefore, it is hypothesized that:

Hypothesis 3. There is no significant relationship between board size and firm performance.

III. METHODOLOGY

3.1 Research Design and Sample

The main objective of this study is to investigation the relationship between three corporate governance components and firm performance within the Nigerian corporate governance environment. Consistent with Kajola (2008); Adenikinju and Ayorinde, 2001; Sanda*et al* and Core, Guay and Rusticus (2005), we consider Earnings per share (EPS) and Return on Equity (*ROE*) as our primary measure of firm operating performance. Tobin's Q (the market value of equity plus themarket value of debt divided by the replacement cost of all assets) which has been used extensively as a proxyfor measuring firm's performance would not be used in this study because information on the market value of debt issued by Nigerian organizations are not available, since these are not usually disclosed in their financial reports. The data used for this study were derived from the audited finance statements of the firms listed on the Nigerian Stock Exchange (NSE) between 2005 – 2010 which comprises of fifteen (15) manufacturing sectors and fifteen (15) financial and service institutions respectively totaling thirty (30) wasfinally used as sample size.Panel data methodology was adopted because it combined time series and cross sectional data.The method of analysis is that of multiple regressions and the method of estimation is Ordinary LeastSquares (OLS).

Table 1.Operational definition of variables

Variable	Measurement Scale
Board independence	This is measured as the percentage of directors who are unaffiliated with the sample firm i.e proportion of outsider directors sitting on the board.
Board Size	Total number of directors on board.
CEO-Duality	Chair duality is an indicator variable taking the value of 1 if the CEO of the sample firm is also the board chair and 0 otherwise.
Earnings per share (EPS)	Net Income – Dividends on preferred Stock / Average outstanding stocks.
Return on Equity (ROE)	Profit after tax / Shareholders' Funds

3.2 Model Specification

The economic model used in the study (which was in line with what is mostly found in the literature) is given as:Organization performance=f(Corporate performance) Organization performance is measured by the following: Earning Per Share (EPS) and Return onEquity(ROE), while Corporate Performance is measured by board independence (BOID); Board size (BOSI) and CEO –Duality (CEDU). Thus, this led to formulation of two separate models each representing a measure of Organization Performance. i.e
Model I $EPS=\beta 0 + \beta 1\ CAR+ \beta 2\ LDR+ \beta 3\ IR+ \beta 4 +Ui$
Model II $ROE=\alpha 0 + \alpha 1\ CAR+ \alpha 2\ LDR+ \alpha 3\ IR+ \alpha 4 +Uii$

IV. PRESENTATION OF DATA ANALYSIS

Table2. Pearson Correlation: Showing the Relations of Corporate Governance Mechanisms and Earning per Share.

Variables	Mean	SD	EPS	BOSI	BOID	CEDU
EPS	43.066	13.840	1			
BOSI	6.000	1.203	-0.012**	1		
BOID	3.666	0.546	0.103	-0.105*	1	
CEDU	0.366	0.490	-0.879*	-0.117*	-0.043	1

Table 2 shows that board size and chief executive duality have negative relationship with earnings per share with (r = -0.012 and -0.879) respectively. Thisindicates that the higher the size of board the lower will be earnings per share and also when chief executive and chairman of the board positions occupied by one person will negatively affect earnings per share. But board independence has positive relations with earnings per share with r = 0.103. This implies thatindependent directors contribute to effective governance by exercising control over top managers' decision-making, because they are seen as the check and balance mechanism to enhance board's effectiveness. Outside directors is considered as true monitors' and can discipline the management and improve earnings per share.

Table 3.Regression Result of Corporate Governance mechanisms and Earnings per Share (N=30)

Variables	Coefficient	T- value	P- value	R^2	F	P	DW-Statistics
BOSI	-0.111	-1.216	0.035				
BOID	0.054	0.054	0.039	0.789	32.483	P<.05	2.363
COE-Duality	-0.890	-9.805	0.00				

Table 3 shows that board size, chief executive duality and board independence were jointly predictor of earnings per share ($F(3, 26) = 32.483$; $R^2 = 0.789$; $P < .05$). The predictor variables jointly explained 78.9% of the variance of earnings per share. It can be deduced from the result that board size ($\beta = -0.111$, $t = -1.216$, $P<.05$); chief executive duality ($\beta = -0.890$, $t = -9.805$, $P<.05$); and board independence($\beta = 0.054$, $t = 0.039$, $P<.05$) were significantly independent predictors of earnings per share. This implies that both board size and chief executive duality have negative significant effect on earnings per share. This means that as board size increases it will lead to increase in communication gaps and cost of coordination and also if the CEO and the chairman of the board is the same person, there would be no other individual to monitor his or her actions, and CEO will be very powerful and may maximize his or her own interests at the expense of the shareholders. But board independence has positive significant impact on earnings per share. This implies thatindependent directors who have knowledge of company affairswould contribute effectively to the earnings per share. These results conform to previous studies (Awan, 2012; Choi et al, 2007; Abor and Adjasi, 2007; Xie et al., 2003 and Naveen and Singh, 2012).

Table 4. Pearson Correlation: Showing the Relations of Corporate Governance Mechanisms and Earning per Share.

Variables	Mean	SD	ROE	BOSI	BOID	CEDU
ROE	13.100	4.851	1.000			
BOSI	6.000	1.203	-0.006*	1.000		
BOID	3.666	0.546	0.065**	-0.105*	1	
CEDU	0.366	0.490	-0.886	-0.117*	-0.043	1

Table 4 shows that board size and chief executive duality have negative relationship with return on equity with (r = -0.006 and -0.886) respectively. This indicates that the higher the size of board the lower will be return on equity and also when chief executive and chairman of the board positions occupied by one person will negatively affect return on equity. But board independence has positive relations with return on equity with r = 0.065. This implies that return on equitywill enhance if independent directors were constituted because they will contribute to effective governance by exercising control over top managers' decision-making.

Table 5.Regression Result of Corporate Governance mechanisms and Earnings per Share (N=30)

Variables	Coefficient	T- value	P- value	R^2	F	P	DW-Statistics
BOSI	-0.097	-1.080	0.040				
BOID	0.016	0.183	0.028	0.795	33.581	P<.05	2.085
COE-Duality	-0.897	-10.009	0.000				

Table 5 shows that board size, chief executive duality and board independence were jointly predictor of return on equity (F(3, 26) = 33.581; R^2 = 0.795; P <.05). The predictor variables jointly explained 79.5% of the variance of return on equity. It can be deduced from the result that board size (β = -0.097, t = -1.080, P<.05); chief executive duality (β = -0.897, t = -10.009, P<.05); and board independence(β = 0.183, t = 0.028, P<.05) were significantly independent predictors of return on equity. This implies that both board size and chief executive duality have negative significant effect on return on equity. This means that the larger theboards sizethe lower the return on equity. This may be as a result of communication gaps and increase cost of coordination. But board independence has positive significant impact on return on equity. This indicates that whenindependent directors who have knowledge of company affairswere put in place the return on equity will be enhanced.These results are in line with kajola, (2008); Dey and Chauhan (2009) and Mark and Kusnadi (2005).

V. CONCLUSION AND RECOMMENDATIONS

This study examined the relationship between corporate governance and organizational performance with special reference to selected Nigerian listed organizations. In general, the results of this study provide evidence that the CEO duality and board size have negative impact on organizational performance (EPS and ROE). In other word, CEO duality is found to decrease the effectiveness of the board of directors because if the CEO and the chairman of the board is the same person, there would be no other individual to monitor his or her actions, and CEO will be very powerful and may maximize his or her own interests at the expense of the shareholders and also the larger the boards size the higher the cost of co-ordination and expense of the shareholders. This study also revealed that only board independence has significant positive impact on organizational performance. It indicates that independent directors contribute to effective governance by exercising control over top managers' decision-making at interest of shareholders. Corporate governance can play a significant role for Nigerian to attract foreign direct investment and mobilized greater saving through long- term debt. Base on this finding, it hereby recommends that the office of chairman and chief executive officer should be occupied by different person in order to enhance check and balance. Small size boards should be encouraged because finding showed that small size boards are positively related to high firm performance. And also board independence should be put in place because outside directors is considered as true monitors' and can discipline the management and improve earnings per share.

REFERENCES

[1] Abor, J. and Adjasi, C. K. D. (2007). Corporate governance and the small and medium enterprises sector: Theory and implications. Corporate Governance, 7(2), 12.

[2] Abdullah, S. N. (2004). Board composition, CEO duality and performance among Malaysian listed companies. *Corporate Governance International Journal of Business in Society*, 4, 47-61.

[3] Abdullah, S. N. (2006). Board composition, audit committee and timeline of corporate financial reports in Malaysia. *Journal of Corporate Ownership & Control,* 4(2), 33-45.

[4] Adenikinju, O and F, Ayorinde (2001): "Ownership structure, corporate governance and corporate performance: The case of Nigerian quoted companies", Unpublished final report presented at the AERC biannual research workshop, Nairobi, Kenya, May.

[5] Awan, S. H. (2012). Effect on board composition on firm performance: A case of Pakistan listed companies. *Interdisciplinary Journal of Contemporary Research in Business*.3(10), 20.

[6] Choi, J. J., Park, S. W. and Yoo, S. S. (2007). The value of outside directors: Evidence from corporate governance reform in Korea. *Journal of Financial and Quantitative Analysis* 42(4) 941.

[7] Duchin, R., Matsusaka, J.G., &Ozbas, O. (2010). When are outside directors effective? *Journal of Financial Economics*, *96*(2), 195-214.

[8] Kajola S.O (2008). Corporate governance and firm performance. The case of Nigerian listed firms.*European journal of economics finance and administrative sciences.*14.16-22.

[9] Naveen K and Singh J.P (2012).Outside directors, corporate government and firm performance. Empirical evidence from India.*Asian journal of finance and accounting*.1(4), 89.

[10] Rahman, R. A. and Mohamed Ali, F. H. (2006). Board, audit committee, culture and earnings management: Malaysian evidence. *Managerial Auditing Journal*, 21(7), 783-804.

[11] Rhoades, D., Rechner, P., &Sundaramurthy, C. (2000). Board composition and financial performance: a meta-analysis of the influence of outside directors. *Journal of Managerial*

[12] *Issues, 12*(1), 76-91.

[13] Schmid, M. M. and Zimmermann, H. (2005). Should chairman and CEO be separated? leadership structure and firm performance in Switzerland. SSRN e-Library. Retrieved from http://ssrn.com/paper.

[14] Shukeri, S. N., Shin, O. and Shaari, M. S. (2012). Does board of directors; characteristics affect firm performance: Evidence from Malaysian public listed companies. *InternationalBusiness Research,* 5(9), 35.

[15] Waseen.M.A, Saleh T.A and Fares J.A (2011). The effect of corporate governance on the performance of Jordanian industrial companies. An empirical study on Amman Stock Exchange.*International journal of humanities and social science*.1(4), 67.

[16] Xie, B., Davidson III, W.N., &DaDalt, P.J. (2003). Earnings management and corporate governance: The role of the board and the audit committee. *Journal of Corporate Finance, 9,*295– 316.

[17] Yermack, D. (1996). Higher market valuations of companies with a small board of directors. *Journal of Financial Economics, 40*, 185-211.

[18] Zong-Jun, W. and Xiao-Lan, D. (2006).Corporate governance and financial distress. Chinese Economy, 39(5), 5-27.