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Corporate Governance: A Theoretical Review

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Abstract

The aim of this paper is to review selected theories of corporate governance. The theories reviewed include the following: Agency Theory; Stewardship Theory; Stakeholder Theory; and Resource-Dependency Theory. The research methodology is anchored on critical narrative literature review which is popularly known as traditional literature review. The review concludes that for the several years, the Agency theory has been one of the major microeconomic trends. It has been applied to banking, industry and the work economy and has been the basis of the economic reward model. For instance, incentives, risk, and employee selection are studied by the Agency. Further, it is concluded that the stewardship theory expresses that stewards ensure and augment investor riches through organization performance. Stewards are corporate chiefs and directors who work for investors and furnish investors with insurance and benefit. Furthermore, it is determined that the nature of Stakeholder theory lies in assumption that the company is a stakeholder system, and these stakeholders operate in a broader system in which each stakeholder and the entire society provide the laws and market infrastructure to allow the company's activities and capabilities to create wealth and shareholder value. In respect of the Resource-Dependent Theory (RDT), it is concluded that Resource dependence theory is concerned with power relations. It analyzes how managers deal with parties that have power over the company because they control resources that the firm needs to operate

Keywords: Corporate Governance Theories; Agency Theory; Stewardship Theory; Stakeholder Theory; Resource-Dependency Theory (RDT).

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1.0 Introduction

The paper presents selected theories of corporate governance which include: Agency Theory; Stewardship Theory; Stakeholder Theory; and Resource-Dependency Theory (RDT). These theories provide the base for a critical understanding of literature which is relevant to the corporate governance and study variables.

1.1 Agency Theory

Corporate governance centres on the division of possession, and this division makes a foremost issue brought about by the partition of organization proprietorship (Berle and Means 2014). Corporate governance is viewed as a framework where the top managerial staffs have set up a significant part to diminish issues influenced by the head operator relationship. Along these lines, the administrator is viewed as the operator, the proprietor is viewed as the head, and the top managerial staffs are viewed as the director (Mallin 2014).

Mitinick (2015) said as per his study that to explain contact between officers and directors, agency theory is used. The agent is the principal in a specific commercial arrangement, and without recourse to self-interest the agent shall represent the best interests of the principal. This relates to the dilemma of the principal investigator. For the past 20 years, Agency theory has been one of the major microeconomic trends. It has been applied to banking, industry and the work economy and has been the basis of the economic reward model. For instance, incentives, risk, and employee selection are studied by the Agency.

Agency theory is one of the principle speculations of corporate governance since it attempts to clarify the job of chiefs in the board. This theory was affirmed by Berle and Means in 1932, and its improvement was credited to the exploration of Alchian and Demsetz (1972). Specifically, the theory believes that companies are useful functions and synchronous operations achieved through market transactions, and that the production of companies is a contract negotiated between individuals to maximize their own interests (Brown and Roberts 2016). Therefore, the theory has a unique view of corporate systems, risks, products, incentives, and it is very common in corporate governance theoretical understanding.

The centre of agency theory is organization relationship, which alludes to an agreement depended on a specialist to lead business exchanges in the interest of chiefs. At that point, the office issue emerges when asking the specialist to take the chief's eventual benefits as the reason. This prompts office costs, including observing expenses and moving specialists to stop misuse (Shleifer and Vishny 2017). Jensen and Meckling (2016) depicted office costs as the aggregate sum of oversight costs brought about by the chief to restrain atypical organization exercises. In light of the contrast between the specialist's judgment and the judgment of amplifying the customer's government assistance, the loss of surplus adds up to a decrease in government assistance. In particular, investors contribute assets for gainful purposes and afterward employ administrators to produce returns for the organization's assets. Along these lines, the connection among investors and chiefs is facilitated through agreements to decide the privileges of administrators and the dispersion of pay inside the organization.

McColgan (2001) advances a more extensive perspective agency theory and corporate governance. The fundamental enthusiasm of his examination is to cover the regions where the interests of managers and investors withdraw. He has been worried about office connections and organization costs brought about by these connections. He expanded crafted by Jensen and Meckling (1976), who characterized the organization relationship as a kind of agreement in which the chief endows a specialist to offer types of assistance. The office issue emerges due to contrasts in interests and clashes among proprietorship and control, in light of the fact that the chief delegates certain dynamic forces to the office. Jensen and Meckling (1976) contend that this sort of appointment power decreases the estimation of corporate supervisors' dynamic amplification.

Himmelberg, Hubbard, and Palia (1999) referred to by Khan (2011) contend that the Principal-agent issue isn't comparative in all organizations, yet is diverse in various organizations, ventures, and societies. Himmelberg et al. (1999) said that Jensen's original theory of "authoritative relationship" additionally suggests a similar view. McColgan (2001) concurs with the creator's view that successful corporate governance instruments can diminish office issues, which is significant for lessening office expenses and friends possession issues. Governance ought to be structured by the professional workplace, on the grounds that a typical system might be more significant for certain organizations, however less significant for other people.

Spanos (2015) suggests that the agency issue relies upon the proprietorship qualities of every nation. Nations with decentralized possession structures work so that if speculators struggle with the board or are disappointed with the organization's presentation, they will utilize leave alternatives, making stock costs fall. The possession structure is minimal, and nations with many controlling investors will in general control the situation of chiefs, in this way constraining the quantity of minority investors and therefore picking up the benefit of private control.

In this manner, the office model infers that gifted individuals can acquire exhaustive data, and financial specialists have capable information on governance exercises and whether they meet the necessities of the governing body (Smallman ,2014). Along these lines, office scholars have presumed that an effective market is the response to how to tackle agency issues (counting the production of a proficient market for corporate purview, work organization, and friend’s data) (Clarke, 2014).

1.2 Stewardship Theory

Contrary to the concept of agency theory, Donaldson (1990) and Davis (1991) proposed a management theory that focuses on maximisation of wealth of shareholders through corporate performance. Subramanian (2018) describes management theory from a psychological and sociological perspective. In the case of what academics call "family business," it is generally used in commercial activities related to the interests of the family business, which has both family managers and shareholders (Miller and Le Breton-Miller, 2006; Braun et al., 2011; Braun and Latham, 2009; Le Breton-Miller et al., 2011).

According to Eddleston, and Kellemanns, the corporate management philosophy is a normative complement to the theory of agencies. This essay claims that the management behaviour, where the interests of the company are consistent with the principles adopted, leads to outstanding corporate governance practises. In the philosophy of management, business management protects and takes action on behalf of investors or shareholders. Its primary goal is to develop and sustain a profitable company such that shareholders can succeed. Management is an ethic of proactive resource control and management. Stewardship principles can be applied to the economy and the environment, economics, and welfare.

The stewardship theory expresses that stewards ensure and augment investor riches through organization performance. Stewards are corporate chiefs and directors who work for investors and furnish investors with insurance and benefit (Sundaramurthy and Lewis, 2003). At the point when the association is effective, the steward will be fulfilled and propelled. It underlines the situation of workers or heads to take more self-governing activities to boost investor returns. Representatives are answerable for their work and buckle down (Hendry, 2002; Shen, 2003).

Gay (2015) expressed that stewardship theory is gotten from a financial model of human conduct; McGregor theory Y clarifies that individuals are brought into the world with an inspiration to work. Along these lines, the theory expresses that there is no contention between the chief and the proprietor, and that a great governance structure permits the organization to arrange with an end goal to improve the interests of the proprietor. The assumption of this stewardship theory is that ranking directors essentially retain the work and life of the organization they are answerable for. In this manner, contrasted and outside directors, they are more disposed to welcome the exercises of the association in a superior manner and can improve decision (Davis, 2016).

Management is propelled to prompt the achievement of the organization in a method of conduct. At the point when directors are acceptable supervisors and serve the interests of investors, checking consumptions will be enormously decreased (Donaldson, 2016). The stewardship theory assists with consolidating the jobs of administrator and CEO, in this manner lessening office expenses and going about as an organization's director. Most definitely, chiefs allude to the directors of the board elements. These elements work for governance to understand the advantages of public governance.

In contrast to the *Agency Theory*, the *Stewardship Theory* of corporate governance developed, providing a distinct perspective that prioritises cooperation and shared goals rather than conflict and competing interests (Glinkowska & Kaczmarek, 2015). The Agency Theory's emphasis on an economic model of human activity is criticised by this theory, which has roots in sociology and psychology. The Stewardship Theory contends that managers, who are frequently referred to as “stewards”, are obliged by nature to act in the organisation's best interests as opposed to their own. This mind-set is the outcome of a sense of duty, commitment, and internal motivation as well as a desire for achievement and recognition. Stewards put in a lot of effort to improve organisational performance and shareholder value because they align their interests with those of the owners. Below are some of the major assumptions of stewardship theory:

Alignment of Interests: When the organisation succeeds, stewards are likely to feel happier and more useful than when they personally gain from it (Schillemans & Bjurstrøm, 2020). The principal-agent conflict predicted by Agency Theory is eliminated as a result of their interests being fundamentally aligned with those of the business and its shareholders.

Intrinsic Motivation: Stewards are motivated by a feeling of duty, professional ethics, and personal fulfilment. As a result, the organisation experiences rigorous effort, dedication, and devotion.

Positive View of Human Nature: Unlike Agency Theory, which presupposes that people have a self-serving nature, Stewardship Theory presupposes that people have an organisational and collective mind-set. Stewards are regarded as accountable, trustworthy, and committed to attaining organisational objectives.

Long-term Orientation: Stewards typically have a long-term outlook, focused on long-term success and expansion (Keay, 2017). Their fulfilment stems from watching the organisation endure throughout time.

Given these presumptions, the stewardship theory advises that organisations create a climate that empowers and inspires managers to participate in stewardship. As part of this, managers should be given more authority, participatory decision-making should be encouraged, and intrinsic rewards should be offered, and a culture of trust and cooperation should be fostered (Keay, 2017). The Stewardship Theory supports arrangements that combine the CEO and chairperson functions because it thinks that doing so will increase the efficacy and efficiency of decision-making. With a focus on interest alignment, intrinsic motivation, a favourable perception of human nature, and a long-term orientation, Stewardship Theory also offers an upbeat view of management behaviour and corporate governance. The theory offers useful insights for improving corporate governance and organisational performance, even though its premises might not hold true in all situations. The need for a relationship-based strategy for corporate governance is also highlighted by stewardship theory.

1.3 Stakeholder Theory

The development of stakeholder theory can be attributed to Freeman (1984). Freeman's research defines the concept of stakeholders and provides an explanation of the corporate responsibility of the stakeholders. The nature of this theory lies in assumption that the company is a stakeholder system, and these stakeholders operate in a broader system in which each stakeholder and the entire society provide the laws and market infrastructure to allow the company's activities and capabilities to create wealth and shareholder value (Clarkson, 1994). Three aspects are involved in the Stakeholder theory, which essentially explain and guide a company’s structure. The descriptive aspect is one aspect and it describes the specificity and specific behaviour of the company. Instrumental aspect is second and it identifies the links between management, stakeholders, and the achievement of the organization's objectives. The third is the regulatory aspect, which focuses on the definition of company functions, such as ethical codes for company operations and management (Donaldson and Preston, 1995).

The study of Freeman (2015) says the doctrine of Friedman is a normative market philosophy advanced by economist Milton Friedman that maintains that the ultimate liability of a company lies with its owners. It is also called the shareholder theory or stockholder theory. The company's aim is therefore to optimise shareholder returns. In principle, a company should generate value not only for shareholders, but for all stakeholders. In 1984, the philosophy of stakeholder management and corporate ethics, which discuss moral and morality in organisational management, was initially defined by Edward Freeman. The corporate governance stakeholder principle reflects on the influence of the corporate sector on all the company's stakeholders. This principle notes that the needs of any player in the governance mechanism should be taken into account by corporate managers (officers and directors). Stakeholder philosophy explores the principles of enterprise, morality and ideals when handling initiative or company stakeholders. It helps to strengthen relationships with partners, thus enhancing project or company efficiencies.

The stakeholder theory joins the board obligation into a wide scope of stakeholders. It was brought up that the chiefs in the association have an assistance arrangement including providers, representatives and colleagues. The theory centres around the board dynamic, the interests of all stakeholders have inborn worth, and it is expected that no intrigue assortment overwhelms different stakeholders.

In Zambia, numerous researchers and policy makers have communicated enthusiasm for breaking down stakeholders as a theory. Li (2012) recommended that corporate governance should comprise formal and casual foundations to build up a proper corporate governance component to profit all stakeholders. Along these lines, the organization will reinforce the suitable dynamic procedure to secure the interests of stakeholders. Li (2011) included that stakeholders in corporate governance can possibly improve the security and advancement of organizations. Yang (2011) accentuated that on the off chance that inside and outer stakeholders get benefits through suitable stakeholder cooperation instruments; at that point the organization can accomplish strength.

Blair (2015) accepts that representatives and various investors are extra daring individuals in the association. Thus, any interest in characterized aptitudes by representatives in the association shows that they have to have a state in the governance of the association. Notwithstanding representatives, clients and providers have a total enthusiasm for the performance of the association. Simultaneously, the nearby network and condition have a genuine enthusiasm for the organization.

Along these lines, the organization should straightforwardly communicate its conclusions to stakeholders on the board and different issues, and assign individuals who speak to minority proprietors, network agents, purchasers, workers, and board providers. Sternberg (2016) called attention to that the stakeholder theory is hoodwinked and wrong since it debilitates individual property, office rights and riches, and contradicts organization tasks and corporate governance. Coleman (2018) additionally concurs that the theory is too prohibitive on the grounds that it just perceives that investors are the main associations in the association that are moderately intrigued by organizations.

In spite of the fact that the stakeholder theory has pulled in antagonistic perspectives, it has advanced into a more unmistakable element since it makes scientists mindful that the association's exercises have left a profound impact on the outside condition, and in this manner proposes obligation regarding numerous individuals' requests. For instance, McDonald and Puxty (2014) anticipated that the organization is not, at this point an investor component, yet lives in a network, so it has commitments to the network.

1.4 Resource dependency theory

This theory is the last supporting theory of corporate governance that the most organisations depend on. It expressed that the foundation of inside corporate governance frameworks, (for example, the top managerial staff) is not basic to guarantee compelling oversight of the executives; however they are a significant connection inside the organization and a significant asset for expanding financial performance (Pfeffer, 2015).

The top managerial staff and non-chief chiefs can give the most significant assets, for example, capable exhortation, shrewd data, freedom and information (Haniffa and Cooke, 2015). They can likewise improve the organization's notoriety and bring significant business contacts (Haniffa and Hudaib, 2015). The third thing they carry is the association with business and political elites, data and capital (Nicholson and Geoffrey 2016). The exact opposite thing the board gives is that the board gives a significant connection between the association's outer condition and stakeholders, (for example, clients and contenders).

It would then be able to be declared that more associations with the outer condition are identified with extraordinary access to assets (Nicholson and Geoffrey 2016), which will positively affect the financial performance of the association. Supporters of this theory accept that the natural association among associations and outer assets is pivotal (Wan and Idris, 2016). These ecological linkages assist associations with decreasing exchange costs identified with the earth (Williamson 2017). The asset reliance theory emphatically accentuates the duty of the directorate in giving asset necessities to carry the association to the following level.

A critical lens for analysing the dynamics of corporate governance in the context of State-Owned Enterprises (SOEs) and their financial performance is provided by Resource Dependency Theory (RDT), which Pfeffer and Salancik first established in 1978. According to the theory, organisations are essentially reliant on the environment in which they function for resources, which forces them to implement methods to lessen this reliance and maintain their survival and profitability. Resources for SOEs include financial and budgetary assistance as well as grants, physical such as “infrastructure and technology”, human skills and expertise, and “informational or data and knowledge” sources (Deng & Yang, 2015). The government, regulators, suppliers, clients, users, employees, and society at large frequently exercise influence over these resources. As a result, the success of SOEs in managing these connections and protecting these resources has a significant impact on their financial performance.

Government as a Key Resource Provider: Because they are state-owned businesses, SOEs are reliant on the government, their largest shareholder, for resources and guidance. Opportunities and difficulties are both produced by this distinctive governing arrangement (Frynas & Yamahaki, 2016). Government assistance can, on the one hand, increase SOEs' financial capabilities, political standing, and market clout. However, it can expose SOEs to political sabotage, ineffective bureaucracy, and competing objectives, which might hurt their financial performance.

Managing Interdependencies: According to RDT, businesses make an effort to control their resource dependencies using a variety of tactics, including vertical integration, diversification, mergers and acquisitions, alliances, and lobbying. The management of these dependencies in the case of SOEs can be greatly aided by good corporate governance processes (Frynas & Yamahaki, 2016). An independent and capable board, for example, can help with strategic decision-making, developing partnerships with stakeholders, and reducing political influence. Similarly to this, strong internal controls can increase responsibility, reduce risks, and maximise resource efficiency.

Balancing Commercial and Public duties: SOEs confront a special problem in juggling their commercial goals with their governmental duties, which frequently results in complicated resource dependencies. Navigating this balance and ensuring that resources are used efficiently to meet goals for both financial performance and public service outcomes depend on effective corporate governance (Esfahbodi, Zhang & Watson, 2016). For instance, a clear business strategy can direct decisions about resource allocation, and performance management programmes can help employees' efforts to coincide with organisational goals.

Engaging Stakeholders: Because SOEs are publicly owned, they have a wide variety of stakeholders, each with their own interests and resources (Esfahbodi, Zhang & Watson, 2016). The ability to access and mobilise these resources, establish legitimacy, and control expectations can all help SOEs improve their financial performance.

Additionally, the Resource Dependency Theory offers a useful framework for comprehending how corporate governance affects SOEs' financial performance. In managing resource dependencies, handling complex mandates, and involving stakeholders, it emphasises the critical significance of governance structures. By utilising the knowledge gained from RDT, SOEs can better their resource management plans, bolster their corporate governance, and boost their financial performance while still carrying out their public service obligations.

2.0 Conclusion

The existence of a conflict of interest between managers and shareholders has increased the attention to effective corporate governance of companies. In this regard, different theories have emerged to understand the whole mechanism of corporate governance, offer different perspectives and solutions to these conflicts, and reduce the problems between stakeholders. This article briefly discusses these theories to better understand corporate governance. In summary, this article describes the basic theories of corporate governance. These theories serve as the basis for better understanding articles related to corporate governance and research variables. As agency theory suggests, the owner-manager relationship provides several governance mechanisms for resolving potential agency conflicts. The management contradiction theory above provides evidence in favour of management and emphasizes that managers work in the best interests of shareholders. Both theories limit the concept of business management to only two parts. Stakeholder theory is interesting because it assumes that all parties have a relationship with the business. He explained that management is accountable to all of the company's stakeholders, not just shareholders. Furthermore, resource dependency theory explains that a company needs certain resources to carry out its activities, which cannot be done without the help of managers or employees. Research on corporate governance has looked at corporate governance scale from many different angles and yielded different results in terms of applicability. It is necessary to explore further the importance of the theoretical foundation of corporate governance in developing countries, particularly, the following theories: Transaction Cost Theory; Political Theory; Sociological Theory

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