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The Effects of Corporate Governance on Firm Financial Performance: A Study of Family and Non-Family Owned Firms in Pakistan

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Abstract
This study examines the effects of corporate governance (Board Size, Board Structure, Leadership Style and Board Meetings) on firm financial performance (ROA, ROE and PM) in family and non-family controlled firms listed in Karachi stock exchange Pakistan. It also aims to find out whether non-family controlled firms perform better than family controlled firms or vice versa. Study employs publicly available data from audited annual reports of a sample of 164 public companies listed in Karachi Stock Exchange for the periods 2006-2011. By using the panel approach, independent samples t-test and multiple regressions using OLS as a method of estimation, the results provide evidence that, non-family controlled firms have significantly higher firm financial performance and governance level then family controlled firms. Corporate governance structure influences the family and non-family controlled companies' performance. Board size and separate leadership style have significant positive impact while board meetings and board structure have negative significant impact on performance. These results are consistent with prior empirical studies. The implication of this study is that the board size should be limited to a sizeable limit and that the post of the chairman and chief executive officer should be occupied by different persons. Non-executive directors should be independent in true sense and role of CEO in the appointment of directors should be reassessed. Regulators need to be vigilant that family and non-family controlled companies practice differently, so they have to set different codes for each type of companies.
Keywords: Corporate Governance, Firm Performance, Family Controlled Firms, Non-Family Controlled Firms, Board of Director

1. INTRODUCTION

Corporate Governance (CG) is the mechanism which includes code of conduct, laws, management techniques, different rules and regulations which direct the affairs of a corporation. These tools are used to protect the individual as well collective interest.

Now the investors and other stakeholders realized that, good CG practices are very important in protecting their interests. In the contemporary business, the key external stakeholders include suppliers, social communities, debt holders, shareholders, customers and trade creditors. All these stakeholders have a direct effect of the corporate decisions. Decisions taken by corporations affect all the stakeholders but only a few of these stakeholders have an influence over the judgments of companies. (Dar et al., 2011; Dar,Naseem, Niazi, & Rehman, 2011; Ehikioya, 2009).

In Pakistan most companies are owned by families. Management of these companies are in the hands of a particular group of family who owned more than 50% of issued capital and have a control over the board and its deliberations. If these companies are not obligated by the force of law or custom to conduct themselves in accordance with the principles of good corporate governance, then interest of all stakeholders and ultimately the entire economy will be adversely affected (Yasser, 2011).

Over the last decade in developed economies the concept of CG is now on priority on the policy agenda and gradually this concept is also becoming a priority in the Pakistan. As a result of this, first time in Pakistan in March 2002 SECP issued a code of corporate governance to ensure the high level of governance structure in listed firms. It was the first effort at governmental level in Pakistan. In line with the best international governance practices the code issued by SECP also include a number of suggestions and recommendations (Dar et al., 2011; Shaheen & Nishat, 2005; Yasser, Entebang, & Mansor, 2011).

Firm performance is a vigorous concept in which all the available financial resources to an organization are used in a judicious way to accomplish the overall objectives of corporate. It not only keeps the company in business but also provide a better prospect for future opportunities (Kajola, 2008). Researchers used a range of financial measures: net profit margin, Tobin's Q, ROA, ROE, ROI, sales, EPS. These performance indicators

further divide in two broad sets: accounting based measures and second is market based measures. The researcher in this study adopted an accounting based measure; return on assets (ROA), Return on equity (ROE) and profit margin (PM) (Anderson & Reeb, 2003; Mollah, Al Farooque, & Karim, 2012;Ujunwa, 2012; Yasser, 2011).

It is very crucial that how family firms are being controlled and directed and as a result of this how much these firms contribute toward the economies of their country (Maury, 2006). Family-owned organizations are the backbone of the economy of the Pakistan. However, either these firms are unaware of the good CG principles or work in a relatively less open environment.

In this study following criteria was defined to detriment family firm:

Family-controlled firm in which (1) Founder is the CEO or successor is related by blood or marriage, (2) At least two family members in the management (3) Family directors have ownership of minimum 20% in the firm. This definition of family firm is consistence with others (Anderson & Reeb, 2003; Lam & Lee, 2012; Mollah et al., 2012; Villalonga & Amit, 2006; Yasser et al., 2011)

1.1 Importance of study

Numerous studies in the literature describe the relationship between CG and performance but unfortunately there are limited studies in Pakistan. CG is on its preliminary stage in Pakistan; the proper application of CG is not exist in abundance at this moment. So this study aims to fill this gap.

We were motivated by a desire to find out whether Pakistani FCF perform better than NFCF or vice versa with regard to CG mechanism, and to aware the people in Pakistan about the benefits of good CG so that, they can get advantage from the opportunities and to compete on both national and international level. This study also make contribution in existing body of literature on corporate governance and this is an empirical research and it used the data of 160 firms listed on the Karachi Stock Exchange (KSE). It will help the policy-makers with the understanding to take proper actions on CG in order to ensure their efficiency and will also be fruitful in field of academics by exploring new ideas and by provide directions.

1.2 Objectives

The objectives of this study are

- To examine the effects of corporate governance in FCF and NFCF in Pakistan.
- To find out whether FCF perform better than NFCF or vice versa.

2. REVIEW OF LITERATURE

2.1 Corporate Governance and firm performance

Mollah et al. (2012) described CG mechanisms are; institution, legal and marketing settings which safeguard outsiders from the opportunistic behavior of mangers and controlling shareholders. Ehikioya (2009) explained that, CG structure like ownership structure, CEO duality, board size and board composition have an impact on performance. The relationship between CG and performance may be positive, negative or no relationship.

Ujunwa (2012) found that, good CG practices are helpful to resolve the conflicts involved in the separation of ownership and control in all over the world. Organizations with high level of corporate governance show better financial performance as compare to those with poor governance structure.

Heenetigala (2011) concluded from his study in Sir Lanka that, even in adverse political and economic conditions, good CG structure was vital to the corporate performance in Sri Lanka.

Black, Jang, and Kim (2003) reported that, CG is a vital factor to explain the market value of Korean public companies. Therefore, effective CG provides superior performance, while poor CG leads to wicked performance. Ashbaugh et al. (2004) asserted that CG mechanisms can improve the performance of firm. Georgiou (2010) conducted his research on FCF and NFCF listed on the Cyprus stock exchange and found that, there is a significant empirical evidence that Corporate governance mechanisms do have a positive impact on the firm value. The implementation of CG mechanisms by FCF can lead to performance benefits. Javed and Iqbal (2007) found that, CG increases the governance level and process of decision making.

Ujunwa (2012) described that, CG negatively influence financial performance. In the opinion of Ponnu (2008) there is a relationship between governance structures and performance. Inferior CG level in any firm is likely to have negative effect on its performance and shareholder's value.

After the analysis Ibrahim, Rehman, and Raoof (2010) derived that, the role of CG is not small and there is significant positive impact of CG on performance. As CG is on its early stages in Pakistan, but due to CG there is a progress in the performance. Tariq and Butt (2008) concluded that, Firms with good CG practices have better financial returns and shareholder value.

2.2 Performance of family controlled and non-family controlled firms

Anderson and Reeb (2003) founded that, FCF performance better than NFCF and it is an effective structure of an organization. One interpretations of superior performance of FCF is that family members know the business and view themselves as firm's steward. Family firms perform better when family member serves as CEO as compare to CEO from outside.

Villalonga and Amit (2006) described that, family control creates value and increase performance of

firm. Ehikioya (2009) by using data from the Nigerian Stock Exchange, found that higher concentrated ownership leads toward the better performance of the firm, since this will motivate shareholders to control and monitor the firm that will result in a greater financial results and market valuation.

Vafeas (1999) concluded that, inside ownership seems to be a substitute for the monitoring activities of board. As per Daily and Dollinger (1992) there is evidence that FCF exhibit an advantage in performance due to the reason that ownership and control are in same hand. He also described that, FCF have long term objectives as compare to NFCF, it focuses on short term objectives as these firms have to fulfill the goals of their shareholders.

Davis, Schoorman, and Donaldson (1997) claimed that, the executives who are considered as the stewards of a company are highly motived to work in the better interest of their firms and principles. As per stewardship theory, managers are not driven by individual goals, but they work as stewards whose motives are associated with the goals of their principals. Stewardship theory describes subordinates as trustworthy, collectivists, and pro-organizational.

Corbetta and Salvato (2004) concluded that, stewardship philosophy is very common in successful FCF. As per Zahra (2005) stewardship philosophy encourage strong involvement and gives a psychological ownership which motivate to work in the best interest of an organization. Chen, Cheung, Stouraitis, and Wong (2005) conducted research in Hong Kong and concluded that there is a negative relationship between FCF and ROA and ROE. Family ownership is not linked with superior financial performance. Lemmon and Lins (2003) described that, firms with family ownership are in a position to exploit the small shareholders.

Ehikioya (2009) derived that when there are more than one member on the board form same family, performance of firm suffer.Chau and Leung (2006) suggested that higher ownership concentration leads towards the dominance of entrenchment effect. As per the evidence suggested by Lam and Lee (2012) FCF does have an adverse effect on performance of public companies in Hong Kong. Non-family owned firms have demonstrated better accounting performance as compare to family owned firms.

Davis et al. (1997) explained that, agency theory describes that, the mangers works as agent (management) of the owners, and their interests may diverge from the interests of owners (principle). In governance research the agency theory is a dominant paradigm. As per agency theory a sensible principal or agent will select the option, which raises his or her own individual utility.

2.3 Board Structure

Hermalin and Weisbach (2001) found no relation between board composition and corporate performance.Anderson and Reeb (2003) concluded that NFCF prevalent more non-executive directors (NED) on the board as compare to FCF. Dalton and Daily (1999) explained that, in the absence of NED the insider dominate and will get massive influence and the board may misuse such powers; on the other hand without the know-how and professional knowledge of the NED, the board may not be effective. As per the code of CG (2002) board should not have more than 75% executive directors.

As per Brennan (2006) non-executive directors are considered as a measure of board vigilance to promote shareholders interest, sometime become debatable. Though the directors, hire and fire executives; but in exercise they are chosen by management. It is also explained that NED are known by CEO and other insiders. NED are suggested by inside and may have relationships with them. Executive directors are more effective as compare to inside directors as they have more information of the firm than the outside directors and they have to rely on executive directors for decision making.

Yasser (2011) found that, board composition the proportion of independent directors on the board has significant negative impact on performance. By implying that, when there is more number of directors on board the performance of firm start to decrease. Firms don't fully use the role of NED. Directors sit on the board just for the fulfillment of requirement of independent directors but they are not independent. According to Coleman & bike pee (2006) found that, board composition has a negative effect on performance in Ghana. Rashid (2009) conducted a research in Bangladesh and found no relationship between NED and performance. NED are not good for firm performance, implying that NED cannot bring any value as they don't have any supervisory position; they have some strong relationship with executive directors and also they don't have sufficient qualification and capabilities.

Lam and Lee (2012) have found weak evidence that, NFCF with a higher proportion of NED attain some inferior market return. Overall; the empirical evidence recommends that the firms with a larger proportion of NED do not overcome others in performance. Fernandes (2005) documented that board structure in terms of the insider-outsider director ratio, the agency theory tends to favor more outsider directors and the firms having non-executive directors suffer less agency problems and have a better alignment of shareholders and managers interest.

Georgiou (2010) after his research in Cyprus concluded that, non-executive directors have significant positive impact on firm value. He explained reasons behind this positive effect of non-executive directors is that, the market takes the inclusion of non-executive directors as a signal of good corporate governance which results

in the increased firm value. The investors relate the high ratio of NED to executive directors on board with more effective monitoring of the activities of the firm and reward these firms with a lower cost of capital; they view all these measures as protecting the shareholders in the firms.

Chau and Leung (2006) recommend that, a positive relationship between the proportion of NED on board an performance of firm and the results also indicate that the positive link between NED and performance is robust for organizations with an autonomous chairman. As per Filatotchev et al. (2005) board independence from founding family has a positive relation performance.

2.4 Board Size

There is a long debate weather board size have impact on the performance of firm or not? On one hand a group predicts board size have a positive impact on performance (Dwivedi & Jain, 2005; Pearce & Zahra, 1992) on other hand a group of researchers says it has negative relation with performance (Hermalin & Weisbach, 2001; Yermack, 1996)

Georgiou (2010) described a significant positive association between size and ROA. He also supports the view that, firms with larger boards are helpful in monitoring the activities of corporation. Dar et al. (2011) conducted a research on oil and gas firms listed on KSE and found that board size have positive relationship with ROE and PM. But this relationship has no significant effect. They also concluded that, size of board should be limited to a sizeable limit.

Kajola (2008) conducted a research on non- financial companies registered on the Nigerian Stock Exchange and found positive relationship between ROE and size. According to Coleman & bike pee (2006) size is positively linked to ROA but negatively to sales growth rate as performance variables.

2.5 Leadership Style

The advocates of the duality of chairman and CEO supports this role by stating that it will help the CEO in quick decision making. On the other side in the light of agency theory this role is criticized on the base of some reasons that it will create hurdles in monitoring the activities of management and it also gives enormous powers to a single individual which may threaten the capabilities of board and such a powerful individual may affect the working and decision making of board like manipulation in board meetings by not raising some important agendas (Rashid, 2009).

Anderson and Reeb (2003) concluded that, with regard to CEO/chairman duality family firms perform better when CEO held two chairs at same time in corporation. It may be due to the reason that family understand business and this involve family members in business to view themselves as steward.

As per study of Georgiou (2010) a positive link exist between CEO/Chairman Duality and performance. When analysis is conducted on the base of firm type then investors don't perceived that duality is harmful for NFCF. There is also lack of evidences which support this notion that duality have any adverse impact on the performance of FCF.

Lam and Lee (2012) found that FCF are expected to demonstrate duality of CEO and Chairman. It has positive effect on ROA and ROE in NFCF but have an adverse effect on performance in FCF. According to OECD, one way to applied the CG mechanisms could be the separation of the roles of chairman and CEO; it will be helpful to board to be in a better position to observe management opportunism (Georgiou, 2010).

Cadbury (1992, p. 21 Para. 4.9), recommends that the roles of chairman and CEO should be separated in corporations. Kajola (2008) described that, there is a positive association between firm financial performance and CEO role. He suggested that CEO and Chairman should be separated so that management could be monitored.

2.6 Board Meetings

Code of Corporate Governance (2002) in Pakistan suggest to board of directors that they should meet regularly after notifying the issues to be discussed. Board of directors should conduct a meeting after each quarter. In the US, yearly six meetings are considered to be a good balance in most of corporation and include some special meetings (Moore, 2002).

There are two schools of thoughts concerning the number of board meetings and performance. One view is that higher number of meetings increases the performance. Other school of thought considers that numbers of board meetings don't assist in enhancing performance or it is inversely related with the performance of firm.

Dar et al. (2011) found that, frequencies of board meetings have positive relationship with performance. But these meetings have no significant relationship. Ward (1991) found that, board should conduct meetings four time in a year and also accompanying monthly meetings of various board committees attended by directors, CEO, and chairman.

Yasser (2011) described that, board meetings have positive impact on performance of FCF. The reason may be that they meet regularly without any time constraint and discussed the issues in detail. In these meetings decisions are take seriously because corporate have to transfer their assets to future generations.

The second school of thought is that meetings are not useful and do not assist in enhancing

performance, as a result of increase in board meetings the performance of fir decrease. One probable reason of this negative impact may be that the agenda for meetings are not set by the non-executive directors; therefore they may be not in a position to raise important issues regarding the improvement of performance.

Vafeas (1999) concluded that, number of board meetings in a year is negatively relate to performance. Boards that conduct higher board meetings in a year are usually linked with poor performance. Share price declines as a result of an increase in the board activities. A handsome cost is linked with board meetings; it includes travel expenses, meeting fees and managerial time etc.

Jensen (1993) found that, the board meetings are not useful because directors spend very little time together and in this time there is no meaningful exchange of ideas with management and among themselves also. The reason may be that CEO sets the agenda of meeting. Task in daily routine may take much of the time in meeting and directors in true sense have low opportunity to exercise their control over the management. In his view, board meetings are reactive measurer but not a proactive measure to improve the level of governance.

2.7 Control variables

As per Rashid (2009) firm size and age have significant positive affect on performance when measured by ROA and negative significant impact on performance when Tobin's Q is taken as dependent variable. Martínez et al. (2007) and Anderson and Reeb (2003) found evidence that the control variables of firm size and firm age, have an significant impact on firm financial performance. They found that there is a stronger performance for FCF as opposed to NFCF when controlling for firm's age and size.

Brennan (2006) describe that, new organizations are likely to have low incomes than older firms due to the reason may be that firm may have less experience and these firms still building their position in market. This recommends that as the firm age increase the complexity of firm increases. Daily and Dollinger (1992) found that, in both FCF and NFCF the firm value decreases as the age increase. Abor and Biekpe (2007) found that, there is a positive effect of firm age on the performance of firm. They conclude that older corporates perform better than younger ones.

3. MATERIAL AND METHODS

3.1 Target population

Target population in this research was listed FCF and NFCF in Karachi stock exchange. A total number of 792 firms were listed in Karachi stock exchange (KSE). These firms are divided into 36 sectors. Some of these sectors were excluded from this research, these sectors include: Bonds, future contracts, stock index future contracts, commercial banks, nonlife insurance, life insurance and financial services.

3.2 Sample size

A sample size of 223 companies from 16 different sectors listed in KSE over the year of 2006 to 2011 was selected for the sake of this research to find out the effects of CG on financial performance. Firms with missing data of different variables were dropped form sample. Extreme values known as outliers (observation that is numerically distant from the rest of the data) were also excluded. Financial institutions were excluded from sample because it is a common practice in the literature. For example Ehikioya (2009); Filatotchev et al. (2005); Coleman and Biekpe (2006); Lam and Lee (2012); Lemmon and Lins (2003); Yermack (1996) gave the reason that CG in financial firms differs from non-financial institution.

As a result 164 companies remain with complete data, required for this research and final sample comprise of 990 firm-years observations for the period of 2006-2011. In this sample 58 companies were non-family owned firms and 107 companies were family owned firms.

Sectors list from which sample was taken

Table 1 Sector Wise List

Sr.NO	Sector Name	Frequency of companies
1	Oil and Gas	12
2	Chemicals	33
3	Automobile and Parts	16
4	Construction and Materials (Cement)	37
5	Tobacco	3
6	Travel and Leisure	5
7	Real Estate Investment and Services	2
8	Pharma and Bio Tech	9
9	Industrial metals and Mining	10
10	Health Care Equipment and Services	2
11	Forestry (Paper and Board)	4
12	Fixed Line Telecommunication	5
13	Electricity	16
14	Beverages	3
15	Food Producers	55
16	Engineering	11

Number of firm in a sector listed on Karachi stock exchange

3.3 Data Collection

The study employs secondary data which is based on the audited financial statements of 164 listed firms on KSE and data collection sources were:

- Basic Balance Sheet Analysis issued by state bank of Pakistan for 2006-2011
- Websites of corporates
- Annual audited financial reports issued by corporations over the period of 2006-2011
- Website of KSE

Data of all independent variables and control variables for the time period of 2006 to 2011 was collected from the audited financial reports of corporates which is available on the corporates websites. Financial data to measure firm financial performance (ROE, ROA and PM) and firm size (total assets of a firm) was collected from basic balance sheet analysis for 2006-2011 issued by SBP.

Time series and cross sectional data was collected for this study. Time series data includes the values of different variables which are being observed over a period of time and cross-section data includes the values for different variables which were collected at same point of time for different variables. To manage this time series and cross section data the statistical technique which applied was panel data approach. Pooled data is also another name of panel data approach, in which for statistical analysis time series and cross-section data is pooled together.

3.4 Variables measurement and definition

3.4.1 Independent variables

Family controlled firm (FCF)

FCF is defined as a firm where Founder is the CEO or successor is related by blood or marriage, or at least there are two family members in management, or a family director holds minimum of 20% ownership in the firm.

Board size (BSIZE)

Board size was taken as independent variable it includes number of directors serving on board of corporation.

Board structure (BSTRUCT)

Board structure was taken as independent variable. It indicates that, how many NED to executive directors are on firm's board. It is a percentage of NED to total number of directors.

Board meetings (BMEETG)

Meetings of the board in a year were taken as an independent variable to check its effect on financial performance it includes the frequency of meetings a year.

Leadership Style: (LSHIP)

Leadership style shows that, either the posts of chairman and CEO and are being held by same individual or by two different individual? If one individual held both seats then it is called as CEO/Chairman Duality, if separately held by different individuals then it is called as separate leadership. It is included as Dummy Variable.

3.4.2 Dependent variables

Return on asset (ROA)

It indicates that, how much profitable a corporation is relative to its total assets. ROA shows that how efficiently management is generating returns from the assets. It is calculated by dividing annual earnings of a corporation by its total assets. When ROA is higher than a firm is able to earn more from low investment.

Net profit margin (PM)

This ratio is achieved as a ratio of profit earned by a company from its sale proceeds. It is desirable for this ration to be high. This ratio gives a measure of net income generated by sale. PM is calculated by dividing company's annual net profit before tax with its total sales.

Return on equity (ROE)

ROE shows the efficiency of firm to generate profits from shareholder's equity it indicates that how a firm employed its resources to generate earnings. ROE is calculated by dividing net profit before tax with average of shareholder's equity.

3.4.3 Control variables

Firm Age (FAGE)

Firm age was taken as control variable in this study. Firm age is the number of years since an organization is incorporated

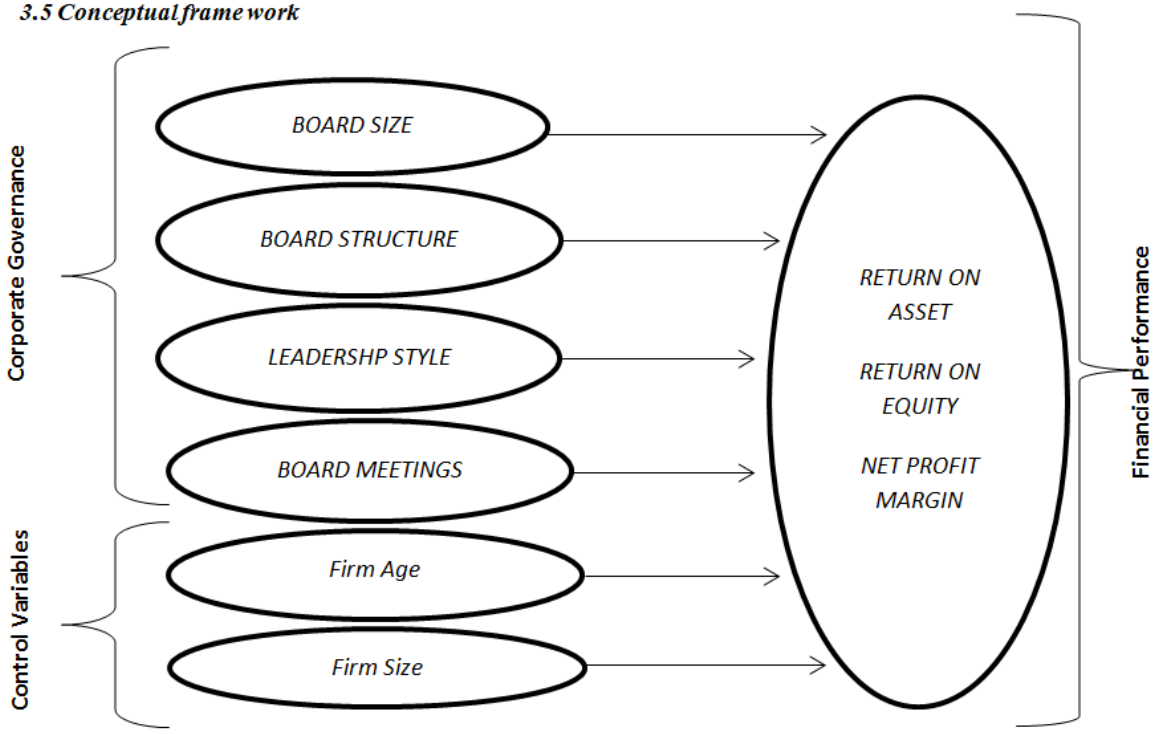
Firm Size (FSIZE)

Firm size indicates the asset base of any firm. It includes total assets, both Non-Current Assets and Current Assets of a firm. As the values were widely dispersed, so for the regression purpose we take log of the total assets.

Table 2 Variables Measurement

Variables	Measurement
INDEPENDENT VARIABLES	
Family controlled Firm (FCF)	(1) Founder is the CEO or successor is related by blood or marriage (2) At least two family members in the management (3) Family directors have ownership of minimum 20% in the firm. It is a dummy variable and coded as 1 if it is a Non family-controlled firm, 0 for Family Controlled firms,
Board Size (BSIZE)	Number of members serving on the board
Board Structure (BSTRUCT)	Number of Non-executive directors×100 Total number of directors
Leadership Style(LSHIP)	It is a dummy variable. Whether firm practice separate or duality leadership. If firm practice separate leadership then it is coded as 1 and when firm practice duality leadership then it is coded as 0.
Board Meetings (BMEETG)	Frequency of meetings per year
DEPENDENT VARIABLES	
Return on Asset (ROA)	Net profit before taxes×100 Average of (Non-Current Assets + Current Assets)
Return on Equity (ROE)	Net profit before taxes×100 Average of Shareholder's equity
Net Profit Margin (NPM)	Net profit before taxes×100 Sales
CONTROL VARIABLES	
Firm Size (FSIZE)	Natural log of total assets. Log (Non-Current Assets + Current Assets)
Firm Age(FAGE)	Number of year since a firm is incorporated.

3.5 Conceptual frame work



3.6 Analytical Technique

The characteristic of the sample size was time series and cross-sectional, therefore panel data regression model was used to check the effects of CG mechanisms on firm financial performance after controlling firm specific characteristics like firm age and firm size in FCF and NFCF. When researcher want to find out the impact or

effect of independent variable on dependent variables then regression model is applied.

Data used in this study were cross sectional and time series so, data are pooled together and panel data regression model was applied for the analysis. Some other names for panel data, such as pooled data (pooling of time series and cross-sectional observations), combination of time series and cross-section data, micropanel data, and longitudinal data (a study overtime of a variable or group of subjects (Gujarati, 2003).

In previous researches Abor and Biekpe (2007); Pietra, Grambovas, Raonic, and Riccaboni (2008); Ehikioya (2009); Martínez et al. (2007); Villalonga and Amit (2006); Yermack (1996) were also applied panel data regression model and found that, the use of panel data regression model provided a good fit in the model when measuring the relationship between CG mechanisms and performance.

In this research descriptive statistics were estimated and more specifically significance testing (that is the t-test) to assess if there were significant differences in the CG and performance variables of FCF and NFCF. The rationale for using descriptive statistics was to identify whether there was a significant differences in variables based on the type of firm and to enable a better explanation of the association between CG and performance of various firms listed on the KSE. T-test was applied to check the validity of results obtained. F-test applied to check the impact of all the independent variables on dependent variable. To check as a whole whether all independent variables have some effect on dependent variable or not?

3.7 Statistical Model

Statistical model developed to analyze the effect of CG variables on firm performance. Statistical model is use to check the relationship between different variables in mathematical equation form.

A total nine panel data regression models were developed for this study, three dependent variables were employed and one model for each variable so three models were developed for whole sample, three models for NFCF and three models for FCF.

The statistical model for this study:

$$Y = \beta_o + \beta 1G + \beta 2C + \mathcal{E} \quad \ldots\ldots (1)$$

Where in equation (1) "Y" is dependent variable represents firm performance; ROE, ROA and PM. "β_o" is constant "β1" is coefficient of explanatory variable (CG mechanisms) and "G" is explanatory variables; Board Size (BSIZE), Leadership Style (LSHIP), Board Meeting (BMEETG) and Board Structure (BSTRUCT), . "C" is vector of control variables; Firm Age (FAGE) and Firm Size (FSIZE) and "Ɛ" is error term.

The equation "1" can be rewritten as:

$$Y = \beta_o + \beta 1X1 + \beta 2X2 + \beta 3X3 + \beta 4X4 + \beta 5X5 + \beta 6X6 + \mathcal{E} \ldots (2)$$

Where:

Y	=	Firm financial Performance = ROA, ROE and PM
β_o	=	Constant
X1	=	Board Size (BSIZE)
X2	=	Board Structure (BSTRUCT)
X3	=	Board meetings (BMEETG)
X4	=	Leadership Style (LSHIP)
X5	=	Firm age (FAGE)
X6	=	Firm size (FSIZE)
Ɛ	=	error term

Panel data regression models for full sample:

ROA = β_o + β1FCF + β2BSIZE + β3BSTRUCT + β4BMEETG + β5LSHIP + β6FAGE +β7FAGE +Ɛ…… (3)

ROE = β_o + β1FCF + β2BSIZE + β3BSTRUCT + β4BMEETG + β5LSHIP + β6FAGE +β7FAGE +Ɛ…… (4)

PM = β_o + β1FCF + β2BSIZE + β3BSTRUCT + β4BMEETG + β5LSHIP + β6FAGE +β7FAGE +Ɛ…… (5)

Panel data regression models for Non-family controlled firms (NFCF):

ROA = β_o + β1BSIZE + β2BSTRUCT + β3BMEETG + β4LSHIP + β5FAGE + β6FAGE +Ɛ…… (6)

ROE = β_o + β1BSIZE + β2BSTRUCT + β3BMEETG + β4LSHIP + β5FAGE + β6FAGE +Ɛ…… (7)

PM = β_o + β1BSIZE + β2BSTRUCT + β3BMEETG + β4LSHIP + β5FAGE + β6FAGE +Ɛ…… (8)

Panel data regression models for family controlled firms (FCF):

ROA = β_o + β1BSIZE + β2BSTRUCT + β3BMEETG + β4LSHIP + β5FAGE + β6FAGE +Ɛ…… (9)

ROE = β_o + β1BSIZE + β2BSTRUCT + β3BMEETG + β4LSHIP + β5FAGE + β6FAGE +Ɛ…… (10)

$$PM = \beta_o + \beta 1BSIZE + \beta 2BSTRUCT + \beta 3BMEETG + \beta 4LSHIP + \beta 5FAGE + \beta 6FAGE + Ɛ \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots (11)$$

3.8 Hypothesis

The main hypotheses developed based on the literature discussed are as follow:

H_1o: Non-family controlled firms and family controlled firms have same financial performance in Pakistan

H_1a: Non-family firms have higher financial performance than family firms in Pakistan

H_2o: Board size has no significant effect on firm financial performance

H_2a: Board size has some significant effect on firm financial performance

H_3o: There is no significant impact of separate leadership on firm financial performance

H_3a: There is a significant impact of separate leadership on firm financial performance

H_4o: There is no significant impact of the proportion of Non-executive directors on the firm financial performance

H_4a: There is a significant impact of the proportion of Non-executive directors on the firm financial performance

H_5o: Board meetings have no significant effect on firm financial performance

H_5a: Board meetings have significant effect on firm financial performance.

To check that whether all independent variables (corporate governance mechanisms) have some impact on dependent variables (firm performance) or not?

H_6o: b1=b2=b3=b4=b5=b6=0

Corporate governance has no impact on firm financial performance

H_6a: b1≠b2≠ b3≠ b4 ≠ b5≠ b6≠ 0

Corporate governance has significant effect on firm financial performance

4. Results and Discussion

Table 3 comparison of FCF and NFCF

The table reports means and standard deviation for different variables of the family and non-family owned firms in Karachi stock exchange based on pooled data for the years 2006-2011. The table also reports the tests of differences in means between family and non-family controlled companies and corporate governance mechanisms with performance indicators.

Source: Developed for this research

	Non Family Controlled Firms		Family Controlled Companies		Difference in Mean	t-statistics
	Mean	SD	Mean	SD		
ROA	14.027	14.703	5.974	11.969	8.053	8.608***
ROE	24.386	29.463	12.586	27.953	11.800	5.768***
PM	10.495	16.195	3.601	15.844	6.894	6.015***
BSIZE	8.648	1.884	7.983	1.405	0.665	5.803***
LSHIP	.866	.341	.758	.429	0.108	3.790***
BSTRUCT	.698	.185	.601	.176	.097	7.558***
BMEETNG	5.121	1.094	5.002	1.232	0.119	1.397
FSIZE	22.678	1.868	21.595	1.522	1.083	9.11***
FAGE	37.687	23.737	32.771	13.459	4.916	3.822***

Notes: *t-test for the difference of means between family firms and non-family firms. Asterisks denote statistical significance at the 1 %(***), 5 % (**), or 10 % (*) level in two-tailed tests. ROA=Net profit before tax divided by book value of average total assets, ROE=Net profit before tax divided by average shareholder equity, PM=Net profit before tax divided by total sales, BSIZE= total number of members on board, LSHIP=Type of leadership that a firm practice, whether separate leadership or duality leadership, BSTRUCT = Percentage of non-executive director divided by total directors, BMEETNG = The frequency a board conducts meetings per year, FAGE = Number of years since incorporated, FSIZE = Natural log of the book value of total assets.*

To assess the differences in corporate governance, financial performance and control variables for the difference in FCF and NFCF, we initially provide descriptive statistics of all the firms, family firms and non-family firms in table 4.2. Significant testing between the means of the FCF and NFCF is shown in above table. FCF and NFCF were significantly different from each other with regard to different performance measures, CG mechanisms and control variables. All variables of NFCF firms are significantly different from FCF, but the mean of board meetings in FCF is not significantly different in NFCF. This shows that both FCF and NFCF have similar number of board meetings in a year.

Table 3 is showing the significant difference between FCF and NFCF for various CG mechanisms,

financial performance and some firm specific variables with t-statistics. For the purpose of mean comparison, independent sample t-test was applied. Results show that on average Return on Asset for NFCF is 14.027% and FCF on average have a Return on Asset of only 5.974%, the difference of 8.053 % between FCF and NFCF is statistically significant at $p < 0.01$. Its means non-family controlled firms have higher Return on Asset as Compared to family firms in Pakistan.

Return on equity on average for non-family controlled firms are 24.386% but for family controlled firms this value is just 12.586 % on average. The difference of 11.800 is highly significant at $p < 0.01$. T-statistics for this difference is 5.768 which show that there is a significant difference between NFCF and FCF. NFCF have higher return on equity then FCF.

Profit margin is also showing similar results like other financial performance measures, on average profit margin in NFCF is 10.495 % and profit margin of family controlled firs is 3.601 %. The difference is significant at $p < 0.01$ and non- family controlled firms showing higher values on all financial performance measures.

Value of board size is also significantly different in NFCF as compared to FCF. On average in NFCF the number of directors on board was 8.648≈9 members, but this value for FCF is 7.983≈8 members. The difference between FCF and NFCF with regard to board size is also highly significant. NFCF practice large board size as compare to family controlled firms. On average 86.6 % NFCF have separate leadership where the post of Chairman and CEO held by two different individual. On the other hand, on average 75.8% family firms practice separate leadership. This difference is also significantly at $p < 0.01$, implying that family firms prefer to have CEO and Chairman Duality as compared to NFCF.

In NFCF on average each firm have a board structure with 69.8% non-executive directors and family firms with 60.1% non-executive directors on board. Again this difference is also highly significant at $p < 0.01$. The board size in non-family controlled firms is 8.648≈9 members and in this board 69.8% members are NED which means in NFCF firms on average out of 9 members there are 6 non-executive members. Results reveled that, NFCF give preference to have more NED on boards as compared to FCF. NED are supposed to bring aspiration and new creative viewpoints, unbiased; having new dimensions of experience, and to improve management accountability by more open discussions (Ward & Handy, 1988).

In family controlled firms board size is 7.983≈8 members in which 60.1% members are non-executive directors on board. It indicates that on average in FCF's board consist of 8 members including 4.8≈5 NED. These figures showing that NFCF prefer to have more NED on board as compare to FCF. Owners of FCF are unwilling to hire NED because they frightened of losing control over the management, and they didn't believe that the NED understand the competitive position of firm (Ward, 1991).

Numbers of board meetings in FCF NFCF on average have approximately same value. In NFCF on average each firm conduct 5.121≈5 meetings in a year. On other FCF have also conduct 5.002≈5 meeting in a year similar to the board meetings in a year as NFCF. The difference is not significant in both FCF and NFCF. This means both FCF and NFCF in a year conduct same number of meetings.

Value of firm size in NFCF is RS 22.678 billion, but in family controlled firms on average firm size is RS 21.595 billion, the difference of 1.083 is significant at $p < 0.01$. It means that NFCF have more assets then family controlled firms. Mean value of firm age in non-family controlled firms is 37.687 years and family controlled firms have an average age of 32.771 years. The difference between FCF and NFCF's age is highly significant. It means that non family controlled firms have larger firm history.

The main conclusions that can be drawn from the compare mean analysis is that, Due to higher ROA, PM, and ROE, investors reward NFCF, that show with higher market value presumably through a decrease in the cost of capital. Further to this NFCF have significantly higher: board size; percentage of NED on the board of directors, and separate leadership. On the basis of these result we will accept our hypothesis $\boldsymbol{H_1a}$ implying that, NFCF have higher financial performance then FCF and $\boldsymbol{H_1o}$ is rejected.

Panel data regression analysis

Table 4

The Panel data regression by using, ROA, ROE and PM (All companies)

Variables	ROA		ROE		PM	
	Coefficients	t-value	Coefficients	t-value	Coefficients	t-value
BSIZE	1.271 (.331)	3.839***	2.084 (.757)	2.751***	1.437 (.354)	4.062***
LSHIP	.415 (1.200)	.346	7.281 (2.961)	2.459**	-3.552 (1.560)	-2.277**
BSTRUCT	-11.263 (2.690)	-4.188***	-15.841 (6.570)	-2.411**	-1.166 (3.327)	-.351
BMEETNG	-.289 (.086)	-3.362***	-.762 (2.53)	-3.010***	-.131 (.048)	-2.699**
OWNERSHIP	9.299 (1.070)	8.694***	8.257 (2.439)	3.386***	4.845 (1.243)	3.897***
FSIZE	-.305 (.311)	-.981	1.855 (.720)	2.576**	.697 (.342)	2.038*
FAGE	.036 (.026)	1.369	.048 (.061)	.785	.041 (.032)	1.271
R Square	.124		.070		.098	
F-statistic	19.464***		8.897***		11.035***	

Notes: *This table presents the coefficients of OLS regression of performance on various corporate governance and firm specific variables in full sample. The values in "parentheses"() are stander error. Asterisks denote statistical significance at the 1 %(***), 5 % (**), or 10 % (*). BSIZE= total number of members on board, LSHIP=Type of leadership that a firm practice, whether separate leadership or duality leadership, BSTRUCT = Percentage of non-executive director divided by total directors, BMEETNG = the frequency a board conducts meetings per year, FAGE = Number of years since incorporated, FSIZE = Natural log of the book value of total assets.*

Table 5

The Panel data regression by using, ROA, ROE and PM (Family and non-family controlled companies)

Variables	ROA		ROE		PM	
	FCF	NCF	FCF	NFCF	FCF	NFCF
BSIZE	2.185*** (.457)	2.178*** (.458)	1.948** (.950)	2.310** (1.045)	1.590*** (.435)	1.358*** (.430)
LSHIP	2.614** (1.291)	2.765** (1.299)	10.087*** (3.364)	4.171** (2.111)	-3.344*** (1.280)	-6.642*** (1.988)
BSTRUCT	-9.826*** (3.287)	-9.385*** (3.295)	-.182* (.108)	-25.068** (10.064)	-.117** (.061)	9.623** (4.243)
BMEETNG	-.339*** (.090)	-.219*** (.065)	-.710*** (.259)	-.205* (.123)	-.048* (.029)	-2.154*** (.751)
FSIZE	-.507 (.385)	-.628* (.383)	.942 (.929)	3.400*** (1.069)	.609* (.369)	1.699*** (.457)
FAGE	.037 (.040)	.039 (.040)	.045 (.80)	.130* (.078)	.156*** (.042)	.017 (.033)
R Square	.072	.068	.048	.121	.079	.166
F-statistic	8.111***	7.645***	4.765***	6.709***	7.178***	10.127***

This table presents the coefficients of OLS regression of performance on various corporate governance and firm specific variables in family and non-family controlled firms. The values in "parentheses" () are stander error. Asterisks denote statistical significance at the 1 %(***), 5 % (**), or 10 % (*).ROA=Net profit before tax divided by book value of average total assets, BSIZE= total number of members on board, LSHIP=Type of leadership that a firm practice, whether separate leadership or duality leadership, BSTRUCT = Percentage of non-executive director divided by total directors, BMEETNG = The frequency a board conducts meetings per year, FAGE = Number of years since incorporated, FSIZE = Natural log of the book value of total assets FCF = Family-controlled companies, NFCF = Non-family controlled firm

In full sample non-family control was taken as independent variable. In full sample with all performance measures the values of coefficient and probability values are (ROA: β=9.299, p =.000; ROE;

β=8.257, p = .001; PM: β=4.845, p=.000). The results show that NFC control has positive significant impact on firm financial performance with all performance indicators and results are in line with (Chen et al., 2005; Filatotchev et al., 2005; Georgiou, 2010; Lam & Lee, 2008, 2012; Mollah et al., 2012; Yasser, 2011). As there is positive impact of NFC on performance we may accept our hypothesis H1a implying that, NFCF have higher financial performance then FCF and H1o is rejected.

Coefficient of board size show positive impact on most of the performance measure. In full sample board size has significant effect on all performance measures (ROA, PM and ROE). Value of coefficients with probability value for full sample with different performance measure is (ROA: β=1.27, p =.000; ROE; β=2.084, p = .006; PM: β=1.437, p=.000). Furthermore both FCF and NFCF achieve higher financial performance with large board size. For FCF value of coefficient and probability value is (ROA: β=2.185, p= .000; ROE; β=1.948, p= .041; PM: β=1.590, p= .000). For NFCF (ROA: β=2.178, p= .000; ROE; β=2.310, p= .028; PM: β=1.358, p= .002). Therefore based on all these results of board size in full sample, FCF and for NFCF alternative hypothesis H2a is accepted and null hypothesis H2o is rejected.

The results discussed above regarding board size clearly indicating that board size has significant effect on the performance. These results also compatible with the view of (Cheng, 2008; Dwivedi & Jain, 2005; Georgiou, 2010; Larmou & Vafeas, 2010; Pearce & Zahra, 1992; Rashid, 2009; Sanda et al., 2005; Yasser et al., 2011). Probable reasons of the positive effect of board size on performance may be that, the current activities of a corporate could easily monitor through large size of board. It may prove a helpful governance tool (Georgiou, 2010; Perry & Shivdasani, 2005). It is expected from a large board that it will bring expertise, intellectuals, people with diverse backgrounds and abilities (Mollah et al., 2012). In large size of board member take decisions after a detail discussion of different issues. That is why there are fewer chances of some extreme decisions and it will lead toward a low variation in the performance (Cheng, 2008). An increase in the size of board will result in the increase in the share price and market may responds favorably to board size increases (Larmou & Vafeas, 2010).

Leadership style/Separate leadership or non-duality has also significant positive affect on performance on all performance measures. In full sample the value of coefficients of separate leadership on different performance measures with probability value is (ROA: β=.415, p =.729; ROE; β=7.281, p = .014; PM: β=-3.552, p=.023). For non-family controlled firms values of beta and probability value is (ROA: β=2.765, p =.034; ROE; β=4.171, p = .049; PM: β=-6.642, p=.001). For family controlled firms (ROA: β=2.614, p =.043; ROE; β=10.087, p = .003; PM: β=-3.344, p=.009). Results indicate that separate leadership has significant positive impact on performance in full sample, FCF and NFCF, when measured by ROA and ROE. But there is significant negative impact on PM in full sample, FCF and in NFCF. Overall a significant effect of leadership style on financial performance this study accepts alternative hypothesis H3a and null hypothesis H3o is rejected for full sample, FCF and in NFCF.

From above discussion it is being cleared that separate leadership has positive effect on performance and these results also compatible with (Braun & Sharma, 2007; Ehikioya, 2009; Kajola, 2008; Ponnu, 2008; Sanda et al., 2005; Yermack, 1996). The expected reason of positive effect of separate leadership may be that it helps the board to perform its monitoring function efficiently. The role of directors is supervisory in nature. Head of management is CEO; if the CEO is also head of board then the true essence of monitoring purpose of board will be lost (Georgiou, 2010).

Agency theory didn't support duality leadership by implying that a single individual with both seats become so powerful. Such a powerful CEO will be a threat to corporate as it may have a undue influence in the affairs of organization like interfering in the formation of committees of board, for the sake of personal benefits not raising important agendas in meetings etc. it may reduce the performance of corporate so separate leadership is ideal for firm (Rashid, 2009). Separate leadership will leads toward optimal performance of firm by enhancing the effective decision making. It also plays a monitoring role to ensure that agent didn't involve in any opportunistic behavior. (Ehikioya, 2009). separate leadership is also encouraged due to the reason that, the CEO and Chairman Duality endorses CEO entrenchment and hinders the performance (Ponnu, 2008).

Board structure has negative effect on financial performance. The coefficients value with probability value of board structure with different performance measures in full sample are (ROA: β=11.263, p =.000; ROE; β=15.841, p = .016; PM: β=-1.166, p=.726). For FCF the value of beta and significance levels for different performance measures (ROA: β=-9.826, p =.003; ROE; β=-.182, p = .092; PM: β=-.117, p=.056). For NFCF (ROA: β=-9.385, p =.005; ROE; β=-25.068, p = .013; PM: β=9.623, p=.024).

The results of board structure in full sample, NFCF and for FCF show that it has significant negative impact on most of the performance measures. More non-executive directors on board will result in decrease in the performance. Overall there is negative effect of board structure on performance therefore we accept alternative hypothesis H4a and null hypothesis H4o is rejected for full sample, FCF and NFCF.

The significant results of board structure are supporting thee view of (Demb & Neubauer, 1992; Lam & Lee, 2012; Rashid, 2009; Sanda et al., 2005; Yasser, 2011). Corporations don't fully utilizing the role of NED.

They sit on board to fulfill the requirements of independent directors but in actual they are just dummies and do nothing. (Yasser, 2011).

Although the directors, hire and fire executives; but in reality they are selected by management. NED is known by CEO or some other insiders. Outside directors are suggested by inside members and they may have relationships with insiders. Executive directors have more information of the firm than the outside directors and they have to rely on executive directors for informed decision making. NED could not add any worth in board because they don't have any supervisory position in board It may be a reason of their negative impact on the performance measure (Brennan, 2006; Paul et al., 2011; Rashid, 2009).

Another reason found in literature that; why non-executive directors have not positive effect on performance? One reason is that, the monetary rewards from the firms to non-executive directors are nominal which give them a little motivation to be seriously involved in a firm's strategy (Bhagat & Black, 1999) One possible explanation for this situation may be that in Pakistan non-executive directors are not independent in true sense.(Butt & Hasan, 2009).

Board meetings have significant negative effect on performance with different performance indicators. In full sample value of coefficient with probability values are (ROA: β=-.289, p =.001; ROE; β=-762, p = .003; PM: β=-.131, p=.007). For non-family controlled firms values of coefficients for different performance measures are (ROA: β=-.219, p =.001; ROE; β=-.205, p = .097; PM: β=-2.154, p=.004). For family controlled firm coefficient of board meetings with different performance indicators are (ROA: β=-.339, p =.000; ROE; β=-.710, p = .006; PM: β=-.048, p=.095).

The results of board meetings in full sample, NFCF and for FCF indicate that; it has significant negative effect on most of the performance indicators. Performance will decrease as a result of more board meetings. Overall there is a negative effect of board meetings on the performance; therefore we accept alternative hypothesis H5a and null hypothesis H5o is rejected for full sample, FCF and NFCF. Results of board meetings are significantly negative; implying that increase in board meetings will result in a fall of performance and these results of board meetings are in line with (Jensen, 1993; Vafeas, 1999; Yasser, 2011).

Some of the important reasons of negative impact of board meetings found in literature are as follow:

There are some costs linked with meetings of board which includes travel, meeting fees and directors expenses etc. Board meetings are reactive, rather than proactive, measures Vafeas (1999). Mostly, the agenda of board meetings are set by chief executive officer of the company and directors of firm could not use the time for some important issues to control over the management and much of time spent on the routine issues which limit the opportunities to the directors Jensen (1993).

The literature reports that, there are some firm specific variables have an effect on performance. Firm size is measured as the natural logarithm of a firm's total assets and firm age includes the number of years since an organization is incorporated. The results of these control variables in full sample family control and for non-family control firm's firm size and firm age in majority of performance measures show positive impact and with significant impact with some performance measures at $p < 0.01$, $p < 0.05$ and $p < 0.1$ respectively. These results of control variables are in line with the previous studies of (Abor & Biekpe, 2007; Ehikioya, 2009; Lam & Lee, 2012; Rashid, 2009; Zahra, 2005)

Suggestion

On the basis of this study it is suggested that:

In Pakistan CG has a significant effect on the performance of both FCF and NFCF. Corporate governance can greatly assist the family controlled firms sector via the introduction of better management practices. Family controlled firms should adopt higher governance mechanisms as NFCF adopted in Pakistan for better performance.

In sum, FCF actually use different strategies. Regulators and investors need to be sensitive to the fact that the CG practiced by FCF differs from that of NFCF in Pakistan. Large board size is suggested for the KSE listed firms; it will be beneficial to discuss the issues in detail with different experts available on board.

In Pakistani perspective, Separate leadership is appropriate as it will helpful to protect the interest of shareholders and all other stakeholders. Duality leadership style gives massive authority to CEO, which challenge the powers of board and make him able to have an undue influence on boards activates.

Non-executive directors are desirable on board and helpful for the monitoring purposes so they are recommended to be on the board. But these NED should be independent in true sense and play role of supervisor in true sense. Regulatory authorities have to review the processes for the selection of NED in order to remove the undue influence of CEO's from the selection process.

Board meetings may play a role in better performance of firm; for this purposes directors should have to spend maximum time to discuss the important issues. Role of CEO in the settlement of agenda of meeting should be neglected. CEO may influence the meetings by not raising an important agenda.

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