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The Effects of the Board on Corporate Performance. Evidence from Cameroon Banks

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Abstract
Using a sample of 10 selected banks annual reports covering 2010-2015, this study examines the relationship between corporate governance and performance in Cameroon banking sector. Based on the econometric model, the result indicates that improved performance of the banking sector is not dependent on increasing the number of executive directors and board composition. It shows further that when there are more external board members; performance of banks tends to be worse. The study concludes a need for increase in board size and decrease in board composition as measured by the ratio of outside directors to the total number of directors in order to increase the bank performance.

Introduction

In today's global economy, the success of the national economy depends on the crucial role of organizations 'competitiveness, transparency and governance structure which operate within her territory, since organizations are the entities that create economic value (ICAN, 2009). Indeed, the need for trust and transparency in the governance of corporate organizations has been one of concern for standard setters all over the world. This need has obviously spurred renewed interest in the corporate governance practices of modern corporations, particularly in relation to accountability and economic performance. Companies concern are increasingly focused toward issues of social content while resolving to maximize economic performance in order to satisfy shareholders and act in a socially responsible manner for the benefit of society as a whole. Social, economic and environmental concern are forcing companies to integrate systems that take in to account the observance of the law in all spheres and also focus on the common goods for society in general and stakeholders in particular. From an academic point of view, there exists an increasing demand in developing business ethics by integrating as research objectives the detection of illicit businesses contrary to social rights (Byrne, 2011). Studies demonstrate that conformation to ethical standards and principles has been an issue persisting through the ages and withstanding the test of time (Michalos, 2008).

In spite of the many research work carried out on the relationship between corporate governance and financial performance, this study still strives to know more and evident the actual relationship between corporate governance and financial performance and also to know to what extend the relationship actually holds in an organization.

A number of research works has been carried out on corporate governance and financial performance both abroad and home but in the case of Cameroon a lot of limitations were faced in this sector due to the lack of qualitative and quantitative data that could give a concrete result on such findings. Corporate governance system is still underdeveloped in most sub Saharan African countries including Cameroon which is still an emerging economy and with the increasingly used method of insider systems. The centralized form of ownership and control of firms in Africa and Cameroon in particular makes it very difficult for firms to expand and also the governance method is not efficient because of no decentralization and separation of ownership and control by firms.

By the analysis of corporate governance system implemented in the selected Cameroonian banks, this study will be able to explain and understand how exactly corporate governance structure can influence individual firms performance.

Presently there exist a relationship between corporate governance and financial performance both from academic and practical point of view. This can be proven by a variety of definitions which will be reviewed in the literature part of this work.

A majority of research work till date on this theme has focused on the relationship between corporate governance and financial performance. Generally, these findings show this relationship to be positive. However, there exists a lack of homogeneity in the results. The reasons are twofold: (1) the absence of a general method that serves as yardstick for comparative studies, and (2) there exists no rigorous method of measuring return on corporate governance (Gjølberg,2009).

The position above could not be separated from prior submission where the growing consensus that good corporate governance has positive link to national economic growth and development. The degree of trust accorded to the managers of companies by its owners is strengthened through corporate governance. Directors without corporate governance mechanism may paint misleading pictures of financial and economic performance of their company to lure unsuspecting investors. Such window dressed accounts raised concern in the U.S.A. with the collapse of the energy corporation ENRON in 2001 which filed for

Bankruptcy after adjusting its accounts (Demaki, 2011). WORLDCOM, GLOBAL CROSSING AND RANK XEROX are other companies in the U.S.A with similar problem. The increasing incidence of corporate fraud relating to exaggerated and fleeting reports have reinforced the renewed global emphasis on the need for effective corporate governance. CBN (2006) reported that despite the significance of good corporate governance to national economic development and growth, corporate governance was still at rudimentary stage as only 40% of publicly quoted companies, including banks had recognized corporate governance in place.

The separation of ownership from the management of business organizations spurs a divergence of interest amongst the parties. The divergence of the interests of the management and its owners has undermined investors' confidence in the Board. Hence, investors are interested about the level of accountability displayed by the Board of directors. The outcry of investors and other stakeholders as a result of mismanagement and inadequate financial disclosures given by the management has deemed it necessary for the institution of sound corporate governance procedures'

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Literature Review

The term corporate governance has been identified to mean different things to different people. Magdi and Nadereh (2002) stress that corporate governance is about ensuring that the business is run well and investors receive a fair return. The corporate governance structure specifies the distribution of rights and responsibilities among different stakeholders in the corporation such as: the board, managers, shareholders, customers, employees, among others, and spells out the rules and procedures for making decisions on corporate affairs. By doing this, it also provides the structure through which the companies' objectives are set and the means of attaining these objectives and monitoring performance. (Uche ,2004; and Akinsulire, 2006). Unlike the above scholars, Nganga, Jain and Artivor (2003) strengthen corporate governance beyond the distribution of rights and responsibilities of different stakeholders with vested interest in corporate organizations to consider the importance of protection of stakeholders, particularly in relation to how well corporate organizations are managed. The scholars define corporate governance as the set of mechanisms through which outside investors are protected from expropriation by insiders (including management, family interests and /or Governments).

A large number of studies have been examined in relationship to corporate governance and financial performance. Most of the studies suggested positive correlation. But despite the intuition that good governance leads to good performance by firm, there has been lack of conclusive evidence on this linkage and the results have been mixed (Pande,2011).

Brown and Caylor (2004) determined that board composition was the most important driving factor among the corporate governance Quotient (CGQ). They also found positive correlation between industries adjusted CGQ scores and financial performance measures-shareholder returns, profitability and dividend payouts and yields. Van de velde et al. (2005) analyzed the linkage of corporate governance ratings and financial performance, and found positive but not significant relationship between them. This observation is consistent with the findings of Gompers et al. (2003) who further found that firms with stronger governance structure and shareholder rights enjoy higher firm value, profit and sales growth. Governance Metrics International and Byun (2006) investigated the association between corporate governance rating financial performance, and found that companies rated in the top 10% of GMI's global data base achieved a higher ROE, ROA, and Return on Capital (ROC) than companies in bottom 10%. Selvaggi and Upton (2008) found that better governance firms yield higher risk adjusted returns. They strongly emphasized that enhanced corporate governance is the cause of enhanced performance and not vice versa . Eisenhofer (2010) concluded that "good corporate governance fosters long term profitability and it does, in fact pay" However, Core et al. (2006) and Statman and glukhov (2009) found no significant association between Corporate governance and financial performance. Azim (2012) used structural equation modeling (SEM) and observed that some governance mechanisms have positive covariance, while some have negative covariance. Thus, he arrived at no consistent and no significant relationship between governance mechanism and financial performance (ROE, ROA Market to Book Value Ratio, Price Earnings Ratio and Dividend Yield) Thus, we observed that some of the existing studies suggested positive and significant relationship; some suggest positive but insignificant relationship; while some studies suggest no significant association between corporate governance and corporate financial performance. Thus existing literature provides mixed and inclusive results and hence, further empirical examination is required to be done in this context to arrive at conclusive results.

The term corporate governance has been defined as the mechanical process of setting rules, laws, regulations and accepted business practices of public and private organizations which govern the organizations between shareholders who invest money in the corporations, on one side and corporate managers who govern the investment and resources, on the other hand (Osisioma and Thomsen, 2005). The investors may include financial institutions and creditors who supply debt finance to organizations whereas shareholders provide equity finance to organizations. On the other hand, employees provide human capital to organizations. In addition, investors also involve suppliers who provide intangible and tangible sources and assets which are crucial for the development and growth of organizations. The concept of corporate governance lies in between all these aspects and management of organizational resources fairly while concerning the interests of all stakeholders (Hermalin, 2005 and Lee, 2008). Contrary to these definitions, Bies (2004) has defined and explained corporate governance as the formal mechanism and the system by which management is held accountable to shareholders for its practices and policies. Contrary to this view, Westhead and Howorth (2006) suggest that corporate governance is the system which defines who are owners and who are the managers of the organization and also defines the regulations and rules for the allocation and management of organizational resources for attaining economic returns on resources and also defines the way of distribution of economic returns to shareholders, employees and managers. Dittmar & Mahrt (2007) have categorized the line of difference between shareholders and managers and also discussed the responsibility of management for managing organizational resources to attain large scale benefits for society and corporation. In another perspective, Eroke (2007) has suggested that corporate governance is the system by which creditors and investors get assurance about adequate and reasonable rate of return on investment.

In this regard, it is arguable that the definitions of corporate governance have proposed different aspects of organizational performance, allocation of resources and ownership structures (Zheka¸2007). In this regard, the definitions of corporate governance have varied from a narrow scope of ownership structures to wider scope which defines the other dimensions of corporate governance such as size and composition of BOD, risk disclosure practices, executive compensation and rules and regulations of organizations. All these aspects have revealed that corporate governance not only assures about allocation of organizational resources but also elaborate what type of ownership structure is to be followed in the corporation. In broader or wider perspective, corporate governance points out the maximization of wealth of shareholders and fair economic growth (Cremers and Nair, 2005).

Authors have reported relationship between corporate governance and performance of organizations. For instance, Thomsen (2005) has noted that strong and effective corporate governance system result in high performance of organizations which also prohibits the fraudulent activities followed in the organizations. Furthermore, Black et al. (2006) evaluate that corporate governance systems and corporate performance are interrelated with each other. In the same vein, Qi et al (2000) have also evaluated that appropriate disclosure of information to stakeholders and strong corporate governance system result in better financial position of organizations.

Empirical evidence on the relationship between corporate governance and performance is mixed. For examples, La Porta, Lopez-de-Silanes, Shleifer, and Vishny (2002) find evidence of higher firm performance in countries with better protection of minority shareholders. Klapper and Love (2003) report that better corporate governance is highly correlated with better operating performance. They also document that firm-level corporate governance provision matter happens more in countries with weak legal environments. Black, Jang, and Kim (2003) provide empirical evidence that there is a positive correlation between corporate governance and performance, but they have no explanation about the causal relationship. Drobetz (2004) also finds that higher corporate governance rating is related to high performance.

However, the above empirical studies are more concerned about examining the differences and correlations than about causal relationships. On the other hand, Drobetz, Schillhofer, and Zimmermann (2003) explore the relationship between firm-level corporate governance and firm performance. They suggest that good corporate governance leads to higher firm valuation (performance), hence, investors are willing to pay a premium, and bad corporate governance is punished in terms of valuation discounts.

Control effectiveness of different types of bank ownerships to moderate the relationships between corporate governance, risk management, and bank performance depend on types of ownerships structure. Types of bank ownerships structure can be classified in different types based on the power of control: shareholders are widely dispersed; a dominant owner who exercises control and appoints management (concentrated); an intermediate case where large shareholders (or called a blockholder) have veto power over major management decisions (Patrick 2001).

Ownership politic is the resource allocation process and reduces the efficiency. Lang and So (2002) examine the composition of ownership structures of banks in emerging markets. They observe that foreign banks have higher holdings than do domestic banks if state stakes are excluded. In terms of bank performance, ownership structure has no impacts on the bank performance.

Goldberg, Dages, and Kinney (2000) compare the bank performance of domestic- and foreign-owned banks in Argentina and Mexico. They find that foreign banks generally have higher loan growth rates than do domestic private owned banks which have lower volatility of lending that contributes to lower overall volatility of credit. Additionally, in both of countries according to them, foreign banks show notable credit growth during crisis periods. In Argentina, they maintain the loan portfolios of foreign and domestically private-owned banks are similar and lending rates analogously respond to aggregate demand fluctuations. In Mexico, they found foreign and domestic banks with lower levels of impaired assets have been similar to loan responsiveness and portfolios. State-owned banks (Argentina) and banks with high levels of impaired assets (Mexico) have more stagnant loan growth and weak responsiveness to market signals. Claessen and Fan (2003) study corporate governance in Asia.

They found that agency problems arise from certain ownership structures. Conventional corporate governance mechanisms (through takeovers and boards of directors) are not strong enough to relieve the agency problems in Asia. Firms use other mechanisms to reduce their agency problems (for example, employing reputable auditors), although they have only limited effectiveness. The low transparency of Asian corporations relates to these agency problems and the prevalence of connection-based transactions that motivate all owners and investors to protect rents. The rents often appear from government actions, including a large safety net provided to the financial sector. Forms of crony capitalism (i.e., the combination of weak corporate governance and government interference) are not only leading to poor performance and risky financing patterns but is also conducive to macroeconomic crises. Their survey suggests that corporate governance in Asia, including Indonesia, remains unresolved problems, both in conceptual and empirical matters of corporate governance in banking sector.

Theoretical Framework

The theoretical framework underlying this work includes a number of different theories. Their distinct approaches are all pertinent in some measure. We can distinguish, on the one hand, the set of theories applicable to the relation between corporate governance and financial performance conforming the conceptual model of our study and, on the other hand, stakeholder theory --- the unique theory --- that supports the relation between Corporate governance and Financial Performance. The integration of these diverse constructs enriches the literature and strengthens the proposed generic model.

Agency theory (Jensen and Meckling, 1976; Fama, 1980; Fama and Jensen, 1983) establishes that the principal(shareholder) and the agent (manager) have opposing interests that may trigger conflicts which will interfere with the smooth running of the company. In contrast, stewardship theory offers an alternative view, which states that there exist ethical and professional motives that will override and prevent conflicts of interest from developing between the principal and agent (Muth and Donaldson, 1998). This latter theory assumes that managers are good resource managers (Donaldson, 1990; Donaldson and Davis, 1991, 1994) who will achieve good business track records thanks to their efforts (Davis et al., 1997); in addition, managers, as honest people (Donaldson and Preston, 1995), endeavor not to hinder the objectives of the shareholders (Donaldson and Davis, 1994) in order to preserve their reputation. Both agency and stewardship theories, in taking the board of directors as principal and the executive body as agent, come into conflict with regard to the consideration of who is responsible for the policies of socially responsible investment and the actions of Corporate governances. The approach offered by the theoretical institutional perspective developed by Scott (2001), which holds that all social participants seek legitimacy and in so doing help develop legitimate rules within the institutional environment (Judge et al., 2010). If companies fix as their objective the quest for legitimacy over economic efficiency (Carver, 2010) and if CG blends in an economic, cultural, and social context, then social welfare and the balance of the interest groups must take center stage (Hess and Warren,2008; Johanson and Östergren, 2010). The descriptive aspect provides a notion for the definition of a company; Donaldson and Preston (1995) describe it as a constellation of cooperative and competitive interests with intrinsic value. From an instrumental point of view, the theory provides the framework for examining the companies and analyzing the relationship between management and the achievement of performance objectives (Surroca et al.,2010); it advocates that companies establish an order of priority amongst its interest groups and favor those who are best positioned. Thus, the level of effort in CSR exercised by companies depends largely on the relative importance of their interest groups (Choi et al., 2010). This contrasts with the normative aspect of this theory, which focuses on the legitimacy of the company's interest groups and the value of their interests, always worthy of attention regardless of category (Kaufman and Englander, 2011). Consequently, it becomes imperative to introduce good CG recommendations as an important element of Corporate governance and financial performance.

Hypotheses

The following hypothesis will be used to determine the analysis and it results.

H1. The board size has a significant positive effect on corporate performance.

H2. The board size has no significant positive effect on corporate performance

H3. There is no significant positive correlation between the degree of board composition and corporate performance

H4. There is no significant positive correlation between the number of executive directors and corporate performance.

Methodology

The study employs basically secondary data from the financial statements of some selected banks in Cameroon. The selection of the banks is due primarily to data availability. Data for the study covers the six-year period from 2010 to 2015

The methodological approach used in most previous work examining the impact of corporate governance on firm performance variables utilizes a multiple regression. Thus, the study employs a modified version of the econometric model of Miyajima et al (2003) which is given as follows:

$$ROA=ao+B1BDS+B2BDC+NED+NNED+BE+eit$$

Where ROA represents firm performance variables; Return on Assets (ROA), for bank i in time BDS.BDC is a vector of corporate governance variables; Board Size (BDS), Board Composition (BDC=number of outside directors/total number of directors), and e, the error term. it is a vector of control variables; Size of the Firm (Size).

Variables and Explanation

The variables for the study were chosen based on data availability and computational purposes.

Firm performance variable.

ROA=this is defined as return on assets and is computed by dividing profits before interest and tax payments by total assets.

Governance variables.

BDS=this is the number of members serving on a firm's board;

BDC=the board composition is the ratio of outside directors to the total number of directors (i.e. number of outside directors divided by total number of directors)

Control Variables

SIZE= this is the size of the firm measured by the value of its asset base. For the regression analysis, we take the log of the assets because the values are widely spread.

The essence of the control variables is to give recognition to the fact that the performance of firms especially banking firms may be influenced by several factors.

The regression is run in a panel manner; various options of panel data regression were run, fixed effects, random effects, OLS and the GLS. The most robust of all was the GLS panel. Thus, we report results of the GLS panel regression.

Data Analysis and Discussion

The data sets are summarized in Table 1, which provides the summary statistics. The correlation matrix between the variables is also provided in Table II.

Table 1: Descriptive statistics of dependent and independent variables.

Variables	mean	Standard deviation	minimum	maximum
ROA	2.2195	1.1012	0	3.48
ASSETS	12.08	4.185	0	14.51
BOARD SIZE	16.2	1.989	15	20
Number Of Executive Director	8	1.71679	5	10
Number Of Non-Executive Director	8.2	1.989	6	11
Board Composition	0.504	0.099	0.4	0.6875

Of the banks studied, the mean board size is about sixteen (16) suggesting that banks in Cameroon have relatively moderate board sizes with a maximum board size of twenty (20) and deviation of 1.98, implying that banks in Cameroon have relatively similar board sizes. The descriptive for the board composition is however low suggesting that the ratio of outside directors to the total number of directors in Cameroon banks is low.

Table 2: Correlation matrix of the variables

Variables	Roa	Asset	Board size	Number Of Executive	Number of Non Executive Director	Board Composition
Roa	1.000					
Asset	0.688	1.000				
Boardsize	-0.306	-0.260	1.000			
Number Of Executive Director (NED)	0.179	0.154	0.432	1.000		
Number Of Non Executive Director (NNED)	-0.461	-0.394	0.628	-0.432	1.000	
Board Composition (BC)	-0.397	-0.335	0.172	-0.814	0.875	1.000

The estimation results are presented in Table III. The variable of number of non-executive directors was removed because of collinearity. This is indicated in the correlation matrix result in Table II above. Overall, the R2, 0.685, suggests high predictive ability of the remaining independent variables. The value indicates that all the included explanatory variables account for about 69 per cent of the variations in the performance of banking industry. Total asset is positive and statistically significant at 5 per cent, indicating that higher total asset has a direct and positive effect on the performance of the banking sector. Board size is positive and significant at 5 per cent level. The result indicates that increase in board size would increase the performance of the bank.

Contrary to studies by Yermack (1996), the study shows that the lager the size of the board, the better the performance. This confirms studies that support the view that larger boards are better for corporate performance because members have a range of expertise to help make better decisions, and are harder for a powerful CEO to dominate and that the larger the size of the board, the better the performance.

However, the coefficient of both numbers of executive directors and board composition is negative but significant at 5 per cent. The result indicates that improved performance of the banking sector is not dependent on increasing the number of executive directors and board composition.

The negative coefficient associated with board composition implies that when there are more external board members, performance of the banks tends to be worse. The result is however consistent with findings by Agrawal & Knoeber (1996) who suggest that boards expanded for political reasons often result in too many outsiders on the board, which does not help performance.

Table 3: Corporate Governance and Performance

Variables	Coefficient	Standard Error
asset	0.1699817*	.0416824
Board size	11.7227*	4.180932
Number of executive directors	-23.17194*	8.216077
Board composition	-366.8878*	129.40
Constant	180.6065	63.22
	R^2=0.6853	

Source: Field Survey, 2013, *, significant at 5 per cent

Conclusion

The study examined the relationship between corporate governance and the performance of organizations from various perspectives: better decision making, effective asset management, better competitive advantage, and improvement in level of confidence, among others. It was discovered that the adoption of good corporate governance practices enhances transparency of company's operations, ensures accountability and improves firm's profitability. It also helps to protect the interest of the shareholders by aligning their interest with that of the managers. The results show that generally corporate governance has positive impact on all the performance indicators of an organization.

The factors of board size, board and management skill, CEO tenure, size and independence of audit committee, foreign and institutional ownership, dividend policy and annual general meeting, all have positive correlation with the performance of organizations. The annual reports and the financial statements of the companies are the main means of communication between the company and the stakeholders. Therefore, the sensitive role of the audit committee by ensuring that the financial statements show the true position of the company's performance cannot be over emphasized. The audit committee must be well constituted to increase its independence and with the right size. Furthermore, the result is an indication that the companies are well positioned to support the economic growth and development of the country. With good corporate governance record, the companies would be able to generate more resources to create more employment opportunities, support businesses through prompt payment of accident claims, pay dividend to shareholders and generate more tax revenue to government.

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