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THE IMPACT OF CORPORATE GOVERNANCE IMPLEMENTATION ON FIRM'S PERFORMANCE IN THE GULF COUNTRIES (GCC) BASED ON STEWARDSHIP ASSUMPTIONS

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ABSTRACT

The purpose of this study is to identify the influence of the corporate governance implementation on the firm’s performance in the countries that belong to the Gulf Cooperation Council. This article is developed based on Stewardship assumptions. The quantitative approach will be used. The quantitative approach will be used to identify the relationship between the study variables. This study sample consisted of the higher ten capital market size companies from each GCC security markets. The SPSS software version 23 is used to analyze the obtained data. The study found out that there is no relationship between Ownership structure, Boards with CEO duality, Executive compensations and the firm's performance in the GCC. While it was found that there are positive and significant relationships between Government ownership, Board size, Board independence and the firm's performance in the GCC. This study was limited to the GCC listed companies. The firm’s performance measurement is limited to ROA, ROE, and EPS. Major implications were found where most of the hypotheses proposed were not supported. The study revealed that there is no significant relationship between the (board independence, board size, ownership structure, CEO duality, government ownership, and executive compensation) and financial performance.

1. INTRODUCTION

In recent years, corporate governance issues have received increased attention among scholars, practitioners and regulators worldwide. It is important to note that there are many players with vested interests in Corporate Governance (CG). These are the shareholders, the management and board directors as well as employees, suppliers, customers, banks, regulators and the general community at large. One can view CG as an overall structure within those companies are directed and controlled. Within this structure, each body has its own commitments and obligations: the boards of directors, for instance, are accountable for the governance of their companies. The shareholders’ role in governance is to select the directors and the auditors. The responsibilities of the board include setting the company’s strategic aims, putting them into effect, supervising the management of the business and reporting to the shareholders on their stewardship. The board’s activities are susceptible to laws, rules and regulations and to the shareholders’ performance in general meeting (Arsalidou & Wang, 2005). Boards that are empowered by a strong CG system exercise better control over the various risks the business encounters (Darmadi, 2013). The members of the board have to ensure high levels of transparency since that help reduce the risk of fraud or theft due to the increased accountability and the likelihood that fraud or theft will be discovered; they should adopt clear procedures and responsibilities for taking important decisions since that guarantees that major decisions are made on a well informed and objective basis; strong CG standards help ensure that the company is acting in the best interests of the shareholders.
The concept of corporate governance refers to the set of principles and rules that govern the design, integration and operation of the governing bodies of the company, such as the three powers within a company: Shareholders, Board of Directors and Senior Management (Arora & Sharma, 2016). Good Corporate Governance provides incentives to protect the interests of the company and shareholders, monitor the creation of value and efficient use of resources by providing information transparency. "The important thing is to emphasize that corporate governance is not an individual instrument but rather a concept that includes the debate on the appropriate management and control structures of companies, as well as the rules that regulate the power relations between owners, the board of directors, management and, last but not least, stakeholders such as employees, suppliers, customers and the general public" (N.R. Narayana Murthy, Chairman of the Committee on Corporate Governance, Board of Securities and Exchanges of India, 2003).
Nowadays, Corporate Governance is as important as efficient financial performance. It is said that around 80% of investors would pay more for a company with a good GC; since this element provides greater security to your investment by ensuring sound corporate practices. The greater the transparency and the more information there is, the greater the confidence of investors in the market (Azeez, 2015). Therefore, the GC is far from being a fad, considering it a necessary concept for the sustainability and growth of companies. The sharp depreciation of oil price globally has driven the oil and gas sector in GCC to adapt the new situation. Most of these sector members have realized that tapers are a signal of risk, which required proactive decisions for re-position itself within the market. Aramco as one of the

largest companies in the oil and gas industry has decided to offer 5% of the company equity for the initial public (Dinesh Nair, 2016). Penetrating the stock market by Aramco will lay a question that what impact might such a listing have on the governance and performance of Saudi Aramco in particular, and on the oil and gas industry in the GCC in general.

2. LITERATURE REVIEW

According to the definition of the World Bank that corporate governance combines legislation, by-laws and relevant practices in the private sector, which allows companies to attract financial and human resources, effectively carry out economic activities and, thus, continue to operate, accumulating long-term economic value for their shareholders, and observing the interests of partners and the company as a whole. The concept of "corporate governance" is not synonymous with the concept of "company management", because it has a broader meaning. Management of the company is the activity of managers who manage the current affairs of the company, and corporate governance is the interaction of a wide range of people in all aspects of the company's activities. In the world, there is no single model of corporate governance as a single principle of building the structure of the company's management bodies. There are two main models (Fan, Wei, & Xu, 2011):

Anglo-American model - typical for the United States, the UK, Canada and other countries. In this model, the management body is a single board of directors, in whose hands the functions of "supervision" and "management" are concentrated. In order to ensure the proper execution of both functions, the board of directors is formed from executive directors who perform the role of managers and independent directors who act as supervisors and strategists. For the same purpose, two types of committees are created in single-level boards of directors such as:

- Operational (for example, executive, financial, strategic) is formed from the number of executive directors to provide management advice. The main function of the operational committees is the combination in the board of directors of the processes of execution of decisions and control over their execution;
- Control (for example, audit, appointment, remuneration) is created from among independent directors with the goal of compliance with the requirements of legality and accountability. The main function of the control committees is to delineate the decision-making process and monitor its implementation.

German model - typical for Germany, the Netherlands (Fan et al., 2011). In this model, the management body has a two-tier structure and consists of a supervisory board, which includes independent directors, and a board that consists of managers. The peculiarity of the German model is a clear separation of the functions of "supervision" and "management" in the company: the supervisory board exercises oversight functions over the executive body, which directly manages the current activities of the company.

There are other differences between the Anglo-American and German models of corporate governance. In the Anglo-American model, the property is heavily "dispersed", the interests of stakeholders (partners) in corporate governance are not represented, outsiders do not have sufficient incentives to participate in corporate control, hostile takeovers are common, etc. The German model, by contrast, is characterized by a concentration of ownership, respect for the interests of stakeholders, control by stakeholders - banks, partners and workers, the lack of hostile takeovers, etc. These models of corporate governance are not mutually exclusive; their elements can be combined by forming mixed models.

Stewardship Theory

Stewardship theory concentrates on psychological and sociological approaches of supervision, rather than the economic instruments of agency theory. The former keeps that institutional members have some shape of affirmative collective identity that causes trustworthy conduct. Donaldson and Muth (1991) argue that financial gain is not the only key role of managerial conduct, and moreover managers need some circumspection to efficiently manage for principals. Therefore, single ownership is not considered as feebleness in stewardship theory as collaborative behaviours are expected to be the covert and inherent conduct of agents, and they are subject to a goal of incentives in addition to financial revenue (Donaldson & Davis, 1991).

Fama and Jensen (1983) investigated that inner board member agents are more probably that outer manager in large corporations because of the deep insight into institutional performances performed by the former. Stewardship theory postulates that concern for their own reputations and career development impedes managers from performing against the shareholders' interests, thereby agency costs should be substantially reduced. The promotion to corporate productivity of stewards refers to the scope in the viewpoint of socio-cultural and psychological elements. For instance, agents are contemplated more probably to implement better with higher authorization and job gratification, which is a psychological element. In general, agents characteristically self-identify as institutional members and thereby contemplate the power accorded them by shareholders to be an instrument to authorize the corporation and other staff to accomplish the goals of the corporation (Fama & Jensen, 1983a).

Table 1: Stewardship Theory Assumptions

As1:	Boards with CEO duality will have higher company performance.
As2:	A higher proportion of executive directors on the board will increase company performance.
As3:	Smaller boards have higher company performance.
As4:	A greater alignment of the interests of board members and the interests of management will lead to higher company performance.
As5:	Boards with directors of lower average age lead to higher company performance
As6:	Boards with higher average tenure lead to higher company performance.
As7:	Boards with a lower level of board independence (based on multiple measures of independence) lead to higher company performance.

3. METHODOLOGY

The targeted data for this study will be retrieved from the annual reports of listed companies in the GCC security market over the period 2007-2016. The quantitative approach will be used. The quantitative approach will be used to identify the relationship between the study variables. Several previous studies have relied on using the correlation and regression tests to figure out the developed hypotheses of corporate governance practices. This study sample consisted of the higher ten capital market size companies from each GCC security markets.

Selecting the sample was based on the higher capital market size, as suggested by several previous studies such as (Chordia, Goyal, Nozawa, Subrahmanyam, & Tong, 2017; Goh, Li, Ng, & Yong, 2015; Pevzner, Xie, & Xin, 2015), it reflects higher contribution to the GDP. Also, higher capital size of these companies enables them to guide the capital market trend, which gives relative result to the study implication and generalize the result.

The data for the corporate governance practices are retrieved from the official websites of each stock market, this data is disclosed within the corporate governance report of each listed company.

The data for the financial performance is retrieved from the database of Thomson Reuters, which disclosed within the annual report of each listed company.

The SPSS software version 23 is used to analyze the obtained data. The correlation test will be used to identify the relationship between each practice with firm performance measures. The correlation test result will clarify the significant and direct of the relationship. The regression test will be used to predict the contribution of each corporate governance practices to the firm performance.

4. DATA ANALYSIS AND RESULTS

Descriptive statistics of the variables used in the analysis are shown in Table 2. Mean is the type of measures of central tendency. The descriptive statistics for the seven countries (70 companies) were calculated separately to identify the firm performance in this study. A summary of the descriptive statistics of the overall data set is presented in Table 2.

The sample consists of 70 firms having state ownership in the year 2004. The mean return on total assets for the sample is 12.9 per cent, while the return on equity on average is 45 per cent. The average earning per share rate is 38.5 per cent. Government ownership in the sample has an average percentage of 10.3 per cent.

A low standard deviation indicates that the data points tend to be close to the mean of the data set, while a high standard deviation indicates that the data points are spread out over a wider range of values. For an approximate result, the coefficient of variation (CV=standard deviation/mean) take into account to identify the variation aspect. As a rule of thumb, a CV >= 1 indicates a relatively high variation, while a CV < 1 can be considered low. However, standard deviations aren't "good" or "bad". They are indicators of how spread out the data is. In this case, all the variables CV is below 1, indicates the variation in the data set used is considered low.

Table 2: Descriptive statistics of variables

	Min	Max	Mean	Std. Dev
BI	0.000	.480	.152	.142
BS	3.000	12.000	5.771	2.008
CD	0.000	1.000	.514	.503
OS	0.400	1.000	.849	.183
EC	9.500	13.740	11.917	1.013

GO	0.010	.173	.103	.038
ROA	0.016	.295	.129	.052
ROE	2.600	6.400	4.50	4.103
EPS	2.690	4.93	3.853	0.569

Note: BI = board independence, BS = board size, CD = CEO duality, OS = ownership structure, GO = government ownership and EC = executive compensation. ROA = Return of asset, ROE = Return of Equity and EPS = Earnings per share.

Table 3 results show all the variables are positively correlated. Hence, the correlation matrix does not indicate multicollinearity where the coefficients are below 0.80. The value in bold indicates that the p-value less than 0.05 and there is enough evidence to reject the Ho of there is a correlation between variables.

Table 3: Correlation Matrix between variables

	BI	BS	CD	OS	EC	GO	ROA	ROE	EPS
BI	1								
BS	-.029	1							
CD	-.281*	.104	1						
OS	.010	.186	.108	1					
EC	.036	-.206	-.116	-.029	1				
GO	.147	-.200	.048	-.134	.035	1			
ROA	.172*	-.185*	-.059	-.173	-.006	.833**	1		
ROE	.007*	-.231*	-.040	-.125	-.038	.587**	.507**	1	
EPS	.172*	.265*	-.133	.015	.127	-.138*	-.172	-.500**	1

*, **, and *** denote the statistical significance at 1%, 5%, and 10% level, respectively.

The establishment and implementation of board independence, board size and government ownership have a positive relationship with the return of the asset. On the other hand, CEO duality, ownership structure and excursive compensation does not directly give an effect to the return of asset where there is no enough evidence to support the hypothesis. In this model, a 10% increase in board independence, board size and government ownership, the return of asset will increase on average by 7.5%, 3.5% and 11.3%. However, 70.9% ($R^2 = 0.709$) indicates that the model explains all the variability of the response data around its mean.

Based on Table 4, the regression results claim that board independence, board size and government ownership is significantly positive to the return on equity and the same time improve the performance of the firm. The results also show a negative coefficient on CEO duality, ownership structure and excursive compensation. On 10% increase in board independence, board size and government ownership, the return of equity will increase respectively by 15.1%, 11.4% and 59.9%. The external variables could explain 38% ($R^2 = 0.38$) variance in ROE of the company.

It was evidence that the same three independent variables; board independence, board size and government ownership prove that there is a positive relationship between earnings per share.

When there is a 10% increase in board independence, board size and government ownership, the earnings per share will increase on average by 3%, 8% and 74%. In this case, the external variables could only explain by 15% ($R^2 = 0.157$) variance in EPS of the company.

Table 4: Result of Regression Analysis

	ROA	ROE	EPS
Constant	0.059	54.094	2.418
	(-1.172)	(1.124)	(2.581)
BI	0.752***	1.514***	0.037***
	(5.214)	(3.689)	(6.127)
BS	0.35***	1.140***	0.085**
	(3.860)	(5.570)	(2.451)
CD	-0.009	-6.363	-0.098
	(-1.235)	(-0.888)	(-0.708)
OS	-0.015	-2.819	-0.133

	(-0.756)	(-0.148)	(-0.360)
EC	-0.003	-3.079	0.098
	(-0.704)	(-0.897)	(1.475)
GO	1.136***	5.999***	0.740***
	(-11.611)	(5.626)	(4.770)
Model Criteria			
Adjusted - R^2	0.681	0.321	0.076
R-square	0.709	0.380	0.157
S.E of Reg	0.295	28.11	0.547
D-W Stat	0.718	0.467	1.020

Note: *, **, and *** denote the statistical significance at 10%, 5%, and 1% level, respectively. Dependent variables = ROA = Return of asset, ROE = Return of Equity and EPS = Earnings per share. BI = board independence, BS = board size, CD = CEO duality, OS = ownership structure, GO = government ownership and EC = executive compensation.

Several studies have addressed the CEO duality-performance relationship, with inconsistent results. Based on Yang.T. & Zhaob.S (2014) provides mixed evidence on the relation between CEO duality and firm performance. Further, their findings justify that the performance difference is larger for firms with higher information costs and better corporate governance. Our results underscore the benefits of CEO duality in saving information costs and making speedy decisions. Doayan, M. (2013) study the impact of CEO duality on the firm performance for a sample of 204 listed firms on the Istanbul Stock Exchange (ISE) between the years 2009-2010 in Turkey. In this study ROA, ROE and Tobin's q used as a financial performance measure. The results show that CEO duality has a negative impact on firm performance.

Lauterbach and Vaninsky (1999) study on the effect of ownership structure on firm performance. This study differentiates between family firms, firms controlled by partnerships of individuals, concern-controlled firms, and firms where block holders have less than 50% of the vote. The empirical work shows that owner-manager firms are less efficient in generating net income than firms managed by a professional manager and that family firms run by their owners perform relatively the worst. This evidence suggests that the modern form of business organization, namely the open corporation with dispersed ownership and non-owner managers, promotes firm performance.

5. CONCLUSION

This research aimed to evaluate the current situation of corporate governance practices in the GCC and to find out whether corporate governance practices have an impact on the firms' performance in the region. The research contained several assumptions and hypotheses were tested based on the secondary data collected to find out the conflict and differences in the corporate governance implementation, practices and firms' performance of the GCC listed companies. These assumptions were based on Stewardship assumptions. The results found that the core role of board independence, board size and government ownership in relation to lead a better company performance. Regression results indicate that the lower level of board independence enhanced the companies' performance. This suggests that small boards are associated with higher firm performance, possibly through closely monitored management. To sum it up, in order to improve the GCC company's firm performance, there are several key factors involved in this study, but out of the six variables only board size, board independence and government ownership play a significant effect role in firm's performance, which is ROA, ROE, and EPS.

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