

ADDIS ABABA UNIVERSITY
COLLEGE OF BUSINESS AND ECONOMICS
DEPARTMENT OF ACCOUNTING AND FINANCE



**THE EFFECTS OF CORPORATE GOVERNANCE ON FINANCIAL
PERFORMANCE OF COMMERCIAL BANKS OF ETHIOPIA**

**THIS PAPER IS SUBMITTED TO DEPARTMENT OF ACCCOUNTING
AND FINANCE IN PARTIAL FULFILLMENT OF THE
REQUIREMENTS FOR THE DEGREE OF MASTER OF SCIENCE IN
ACCOUNTING AND FINANCE**

BY: ZENEBECH KOROTO KOYRA

ID NO.: GSE/2124/15

ADVISOR: TEMESGEN W. (PhD.)

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ADDIS ABABA

DEDICATION

This thesis is dedicated to my beloved late elder brother, Dr. Tadiwos K.

DECLARATION

The thesis titled “**The Effects of Corporate Governance on Financial Performance of Commercial Banks in Ethiopia.**” is entirely my own creation, I, Zenebech Koroto Koyra, therefore declare. With the help and direction of my advisor, I completed the research for my thesis on my own. This research has not been submitted for any degree or diploma at this school or any other. It was completed in order to fulfill a prerequisite for the Master of Science in Accounting and Finance.

Name: Zenebech Koroto Koyra

ID No.: GSE/2124/15

Signature: _____

Date: _____


20/6/2025

ADVISORS' APPROVAL SHEET
ADDIS ABABA UNIVERSITY
COLLEGE OF BUSINESS AND ECONOMICS
DEPARTMENT OF ACCOUNTING AND FINANCE

This is to confirm that Zenebech Koroto Koyra worked under my direction and supervision to complete her research project on the subject of **“The Effects of Corporate Governance on Financial Performance of Commercial Banks in Ethiopia.”** By signing this document, I vouch for the suitability of her work to be submitted for the Degree of Master of Science in Accounting and Finance.

Temesgen W. (PhD.)

Name of Advisor


Signature

24/06/2025

Date

ENDORSEMENT AND APPROVAL

As Thesis research advisor, I hereby certify that I have read and evaluated this Thesis prepared, under my guidance, by Zenebech Koroto entitled "The effects of Corporate Governance on Financial Performance of Commercial Banks in Ethiopia." This is rectified to be submitted as fulfilling the Thesis requirement.

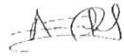
Temesgen W. (PhD.)
Advisor


Signature

24/06/2025
Date

As member of the Board of Examiners we have read and examined the thesis prepared by Zenebech Koroto. We agreed that it be accepted as fulfilling the thesis requirement for the degree in Masters of Accounting and Finance.

Name: **Abebaw Kassie (PhD)**
Internal Examiner


Signature

24/6/2025
Date

Name: **TIGIST BELACHEW (PH.D)**
External Examiner


Signature

26/06/2025
Date

Name: _____ Signature: _____

Date: _____

Dean of AAU FBE Campus
Faculty of Business and Economics

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Conceptual

LIST OF ABBREVIATIONS AND ACRONYMS

AB	Awash Bank
BOA	Bank of Abyssinia
CBE	Commercial Bank of Ethiopia
COOP	Corporative Bank of Oromia
DB	Dashen Bank
NBE	National Bank of Ethiopia
OP	Organizational Performance
S.C.	Share Company
SPSS	Statistical Package for Social Science

Abstract

This study investigates the effects of corporate governance mechanisms on the financial performance of commercial banks in Ethiopia. In light of the increasingly complex and regulated financial environment, sound corporate governance has emerged as a critical determinant of organizational performance, especially in banking institutions that face heightened agency problems due to information asymmetries. Drawing on agency theory, stakeholder theory, and resource dependency theory, this study employed a mixed-methods research design, combining quantitative analysis of panel data from 2019 to 2023 with qualitative insights gathered through interviews with board members from five major commercial banks in Ethiopia. The study examined six key governance variables—board size, board meeting frequency, board gender diversity, directors’ educational qualifications, directors’ industry experience, and chief executive officer (CEO) compensation—and assessed their influence on bank performance, as measured by return on assets (ROA). The regression analysis revealed that board size, frequency of board meetings, educational qualifications of directors, and industry-specific experience were positively and significantly associated with financial performance. However, gender diversity and CEO compensation showed no statistically significant effect. The findings underscore the importance of strengthening governance frameworks tailored to the unique structural and regulatory environment of the Ethiopian banking sector. This research provides empirical evidence to inform policymaking by the National Bank of Ethiopia and bank shareholders, and contributes to the literature on corporate governance in emerging economies, highlighting the context-specific nature of effective governance structures. It also offers practical implications for aligning governance reforms with performance enhancement in the Ethiopian banking industry.

Keywords: Corporate Governance, Financial Performance, Commercial Banks, Ethiopia, Board Structure, Return on Assets, Agency Theory, Mixed Methods.

CHAPTER ONE

INTRODUCTION

1.1. Background of the Study

Since the beginning of time, the biggest challenge facing humanity on this planet has been the intractable problem of risks and uncertainties, which has remained unresolved despite the tremendous advancements in science and technology over the years. The international financial landscape is changing rapidly; economics and financial systems are undergoing traumatic years. Globalization and technology have continuing speed, financial arenas are becoming more open with new products and services being invented and regulators everywhere are scrambling to assess the changes and master the turbulence. (Ranti & Samuel, 2012). According to (Ranti & Samuel, 2012) (as cited in (Kaheeru, 2001) in this brave world, one fact remains unchanged. There is a need for countries to have sound resilient banking systems with good corporate governance, which will strengthen and upgrade the institution, to survive in an increasing open environment. Sound corporate governance in the sectors is essential to the realization of the aforementioned benefits of banks. The business community, regulators, and capital market authorities are beginning to acknowledge governance as a key factor influencing corporate performance. Therefore, corporate governance is designed to carry out a system of oversight that employs strategies like board structure, duality, reporting, and compensation to give shareholders the information they need to hold management accountable for their choices. Husam and associates (2012).

Corporate governance, according to Edwards & Clough (2005), is an organization's commitment to implementing just and moral policies throughout its entire system and in all of its relationships with a wide range of stakeholders, including shareholders, suppliers, customers, and the government. It concerns the systems and procedures put in place to support and oversee efficient organizational administration, including safeguards against compliance and prevent unlawful and improper behavior.

Cadbury (2003) reiterated this by stating that corporate governance is all about preserving a balance between social and economic objectives as well as between individual and group objectives. The primary purpose of the governance system is to encourage the best possible

use of resources and to hold resource stewards accountable. Corporate governance is also defined by the Organization for Economic Cooperation and Development (OECD) as the entirety of the connections between a company's shareholders, board, management, and other stakeholders. It gives the organization the framework for establishing its goals, figuring out how to reach them, and keeping track of its progress. The history of corporate governance systems is now well documented from a worldwide standpoint. However, over the last 20 years, corporate governance arrangements have undergone substantial changes, which have raised scholarly interest in the board of directors' role in influencing company success (Gomez, 2005). The legitimacy of the current corporate governance structures has been questioned as a result of numerous high-profile company failures and generally poor corporate earnings worldwide. Thus, more attention should be paid to the current corporate governance structures and how they provide accountability and responsibility, according to later studies (Shleifer and Vishny 1997).

According to Ongore and K'Obonyo (2011), the well-known cases of Enron Corporation, Adelphia, Health South, Tyco, Global Crossing, Cendant, and WorldCom, among others, have been frequently cited as typical scandals that support corporate governance reform and the need for new procedures to combat the alleged abuse of power by top management.

Multidisciplinary empirical research studies on the effect of different corporate governance mechanisms on firm performance have significantly increased during the past ten years. Studies of corporate governance concerns have drawn a lot of attention in the accounting and finance literature and have been utilized as markers of a company's success or failure. Additionally, studies show that organizations with strong corporate governance practices appear to have greater success than those with weaker practices. Khaled and associates (2007).

Several studies have suggested that when markets are ideal, businesses should act in the best interests of their shareholders. This isn't the case with developing markets, though, which are unfinished and flawed. According to corporate governance researchers (Huse, 1995; Gomez, 2005), there is still disagreement about the best corporate governance framework that could protect shareholders' assets and encourage wealth-building endeavors.

Positively, there was an increasing recognition that better corporate governance was essential to the expansion and advancement of a nation's entire economy (Clarke, 2011). Additional research revealed a high correlation between the performance of corporations and their boards' governance procedures (OECD, 1998; Tornyeva et al., 2012; Nasar Najjar, 2012; Almanasser et al., 2012). However, David et al. (2013) found no evidence of a substantial correlation between the governance procedures of boards and the performance of enterprises.

Any financial system must have banks because they are essential for transferring surplus sector savings to deficit sectors. The banking industry dominates the Ethiopian financial sector. Since the effectiveness and competitiveness of the banking sector determine the strength of any economy, banks are essential to Ethiopia's economic development and change. The banking industry in Ethiopia consists of seventeen commercial banks, sixteen of which are privately held, and one development bank. Mulugeta (2010) identifies interest rate regulation, credit limits, equity market regulations, and foreign exchange controls as the main regulatory aspects.

Mulugeta (2010) states that Ethiopia has developed a strategic framework for the financial sector and emphasizes the need to improve the capacity of professionals in the financial sector as well as strengthen corporate governance and accountability of financial institutions. The Central Bank of Ethiopia oversees and directs the banking industry, regulates the nation's money supply, and keeps an eye on the financial performance of five private commercial banks in Ethiopia.

To this end, this study examines the effects of corporate governance mechanism and financial performance of commercial banks in Ethiopia. This will not only add to existing literature but also it will serve stakeholders to handle potential multi conflicts in the sectors.

1.2.Statement of the Problem

According to Khaled and associates (2007), relationships between shareholders, board members, management, employees, and other stakeholders with whom the company has business ties are determined by corporate governance standards. It primarily outlines the responsibilities and safeguards the rights of the business and the aforementioned participation groups. Thus, establishing the rights and responsibilities of the aforementioned groups and maintaining investor confidence depend on corporate governance rules.

Commercial banks are corporations that have a dominant position in developing economic financial systems, and they are important engines of economic growth of a country (Levine, 1997). Banking failure would affect the entire financial system and economy of a country. Therefore, in order to ensure the improvement of the company performance, economic efficiency and growth, and to enhance investors' confidence; strong, effective and good corporate governance has to be developed and implemented.

Most previous studies like conducted by Yasser (2011), Al-Manaseer et al. (2012), and Kyereboah Coleman (2007) have been undertaken on large firms operating within well-organized corporate governance mechanisms in developed economic system and in countries where there are capital markets. When we see developing countries specifically in Ethiopia some studies on corporate governance have been conducted previously. But corporate governance mechanisms were not covered sufficiently by those studies. And the number of observations was limited in those studies. To mention some of the observations' limitations: Using narrow period or number of years and small sampling size. Methodology of data gathering and analyzing focused by some of the studies were limited only on secondary data. In addition, this study focuses on the privately owned commercial banks since majority of banks in Ethiopia are those banks and they are significantly differs on some aspects as compared to the government owned commercial banks. And most of our private commercial banks are almost at the same size, level or category and may help in order to reach on reasonable results. This also could help to see their linkage with the corporate governance mechanisms. Previously there were no any studies conducted by focusing only on privately owned commercial banks. Therefore, it is difficult to generalize the same result from the findings of the studies that were done in developed countries, for relatively small size Ethiopian private commercial banks governance mechanisms. Ethiopian banking sector's corporate governance is characterized by the absence of an organized share market and the country has different rules, regulations, practices, and economic features which needs to conduct a separate study using various perspectives, meaning they were concentrated on agency theory which is the central need to cooperate governance are to protect the interest of shareholders only have not been conducted within a well-organized corporate governance mechanism. This study has been conducted to provide empirical evidence particularly on the

effect of corporate governance mechanisms on privately owned commercial bank's financial performance.

To come up with a better insight; this study covers by assessing and including selected corporate governance mechanisms major areas of board of director characteristics, regulation aspects, shareholder and depositor related issues (specifically the independent variables: Board size, board gender diversity, directors educational qualification, directors' industry related experience, chief executive compensation). Hence this paper sought to determine the relationship between selected corporate governance mechanisms, which have been sufficiently uncovered variables in the previous studies in order to further be explained and financial performance of the private commercial banks with in the given period of time which was measured by the return on asset (ROA).

Despite the growing body of international literature on corporate governance and its influence on firm performance, most of these studies have been concentrated in developed economies with well-established regulatory frameworks and capital markets. The findings from such contexts may not be directly transferable to developing economies like Ethiopia, where financial systems are less mature, and institutional governance mechanisms are still evolving. Moreover, in Ethiopia, existing studies have largely focused on general legal and institutional aspects of corporate governance or ownership structures, with limited empirical analysis on how specific internal governance mechanisms—such as board structure, educational qualifications, gender diversity, and executive compensation—affect the actual financial performance of commercial banks. Few studies, such as those by Minga (2008), Fekadu (2010), and Ahemad (2012), have touched on governance-related issues, but they lack recent, sector-specific, and data-driven investigations. Additionally, previous research has not adequately captured longitudinal performance data or employed a mixed-method approach to triangulate board-level insights with quantitative performance metrics. This creates a significant knowledge gap that the current study seeks to address by providing context-specific empirical evidence using recent data and directly engaging board-level decision-makers in Ethiopia's leading commercial banks.

This study fills the gaps and serves as points of reference for further research in corporate governance and provides empirical evidence on the effect of corporate governance

mechanisms on financial performance of the banks by taking in to consideration the variables, observations and sampling methodologies related to the realities of the banks governance mechanism in Ethiopia.

1.3.Objectives of the Study

1.3.1. General Objective of the Study

The general objective of this study is to examine the effect of corporate governance on financial performance of Ethiopia commercial banking industry in controlling the influence of some selected commercial banks specific variables using five years data 2019-2023.

1.3.2. Specific Objectives of the Study

Given the overall objective of examining the effect of corporate governance mechanisms on firms' financial performance using some selected commercial banks in Ethiopia, this study had several specific objectives. Specifically, the study sought to:

- a) Investigate the relationship between board size and bank performance.
- b) Examine the association between board frequency of meeting and bank performance.
- c) Examine the association between board gender diversity and bank performance.
- d) Ascertain the influence of the directors' educational qualification on bank performance.
- e) Identify whether directors industry related experience affect bank performance.
- f) Ascertain influence of chief executive compensation on bank performance.

1.4. Research Hypotheses

Using the literature reviews as a guide, the researcher came up with the following hypotheses:

H1: Board size has a positive and significant effect on Bank Performance.

Several studies suggest that a larger board can bring diverse expertise and experience, enhancing strategic decision-making and oversight. Uadiale (2010) found a positive relationship between board size and financial performance in Nigerian companies. Similarly, Al-Sahafi et al. (2015) concluded that larger boards are positively associated with higher ROA and ROE in Saudi banks. However, others like Samuel and Ranti (2012) found a negative relationship, citing coordination difficulties in larger boards.

Despite mixed evidence, the prevailing view in bank governance literature in developing countries supports a positive role for moderately large boards in enhancing performance.

H2: Board frequency of meeting has a positive and significant effect on Bank Performance.

Frequent board meetings allow directors to better monitor management and respond proactively to emerging risks and opportunities. Ntim and Osei (2011), in their study of South African firms, found a significant positive correlation between board meeting frequency and firm performance, supporting the agency theory's premise that active oversight reduces agency costs. Although studies such as Akpan (2015) and Johl et al. (2015) reported a negative effect due to increased costs, the balance of evidence—especially in financial institutions—suggests frequent meetings are beneficial for governance and performance.

H3: Board gender diversity has a positive and significant effect on Bank Performance.

Gender diversity is considered beneficial for improving board dynamics, inclusiveness, and decision-making. Erhardt et al. (2003) found that gender-diverse boards are linked to improved performance due to enhanced dialogue and alternative perspectives. While Rose (2007) and Shafique et al. (2014) found no significant effect, the theoretical underpinning from stakeholder theory emphasizes fairness and representation, which justifies testing the positive effect of gender diversity in governance effectiveness.

H4: Directors' educational qualification has a positive and significant effect on Bank Performance.

Highly educated directors are presumed to bring advanced skills, analytical ability, and strategic insight to board functions. Poon, Heong, and Lee (2013) demonstrated that firms with board members holding academic and professional qualifications in relevant fields achieved better financial outcomes. Ferreira (2010) also emphasizes that well-educated directors enhance the board's capability to oversee complex financial institutions. This supports the hypothesis that higher educational attainment among directors contributes to improved bank performance.

H5: Directors industry related experience has a positive and significant effect on Bank Performance.

Experience in the finance or banking sector equips board members with practical insights and a deeper understanding of market dynamics, risk management, and regulatory compliance. DeZoort et al. (1998) and Ferede (2012) both found that directors with industry-specific expertise positively influence firm performance, especially in financial institutions where domain knowledge is crucial. Resource dependency theory also supports this, as experienced directors act as valuable assets for strategic guidance and environmental adaptation.

H6: Chief executive Compensation has a positive and significant effect on Bank Performance.

Agency theory posits that aligning CEO compensation with firm performance reduces agency problems and motivates executives to act in shareholders' interests. Studies like Jeppson et al. (2009) and Haid and Yurtoglu (2006) support a positive pay-performance relationship. However, some evidence (e.g., Fernandes, 2005) suggests weak or insignificant effects. Nevertheless, considering Ethiopia's evolving corporate governance landscape, investigating this link is important to understand whether compensation incentives drive financial performance in the banking sector.

1.5. Significance of the Study

It is anticipated that many participants in Ethiopia's many sectors will find particular value in the study's conclusions.

By identifying pertinent internal corporate governance mechanisms and how they affect financial performance, the study's findings will benefit the banking sector. The findings of this study add to the body of knowledge by demonstrating the connection between the financial performance of commercial banks and internal corporate governance mechanisms.

The empirical findings would also serve as broad indicators of corporate governance mechanisms that the shareholders of commercial banks and the National Bank of Ethiopia might utilize to inform their policy and decision-making, since it implies which corporate governance aspects should be prioritized to enhance financial performance of commercial banks.

More additionally, study serve as a stepping stone for future researchers and suggests areas where gap in literature exist, where further research studies are required so that scholars in the field of finance and Economics can do further studies of them.

1.6. Scope of the Study

The scope of the study is restricted to examine effects of corporate governance mechanism on financial performance of banks that are registered by the NBE and that has operated at least five years. To this end, this study were limited to internal corporate governance mechanism variable (board size, Frequency of board meetings, Existence of female directors in the board, director's educational qualification, director's industry specific experience, and Chief executive compensation) as explanatory variable and the controlling variable were delimited to premium growth rate to see their effects on financial performance. The dependent variables were delimited to return on asset. The secondary data used were collected for the period of 2019-2023.

Hence, all of the research's analysis and outcomes are restricted to the case study location that was chosen, and the findings' conclusions and outcomes may not apply elsewhere.

1.7. Organization of the Study

There are five chapters in the study: The first chapter includes an introduction section and concentrates on the following topics: study background, problem statement, research questions, aims, research hypotheses, importance, and study organization. The second chapter incorporates an assessment of the relevant literature and focuses on relevant theoretical and empirical reviews for this investigation. The third chapter includes a methodological section that concentrates on the following topics: the research design, data type and source, the study's target population, sample size and sampling methods, methods of data collection, methods of data analysis, reliability and validity analysis, and ethical considerations. The demonstration, investigation, and explanation of data are all included in chapter four. Finally, last and the fifth chapter incorporated the research's results deductions and suggestions.

CHAPTER TWO

REVIEW OF THE RELATED LITERATURES

Introduction

This chapter review about corporate governance, theoretical framework related to corporate governance. It also analysis the literature related the effect of corporate governance on firm performance. Empirical studies and hypothesis development also review on this chapter.

2.1. Meaning of corporate governance

A set of open and honest connections between an organization's management, board, shareholders, and other stakeholders is provided by the antiquated idea of corporate governance (Kotnal, 2016). According to Kaplan (2015), corporate governance is a framework that directs and controls businesses in the best interests of stakeholders, including shareholders. In order to promote excellent corporate governance, corporate governance entails establishing credibility, guaranteeing accountability and transparency, and keeping an efficient information disclosure channel (Ranti & Samuel, 2012). Corporate governance, according to Andrei and Robert (1997), is concerned with how companies' financial providers guarantee that they will receive a return on their investment. These guarantees are central to the concept of effective corporate governance, according to Holly and Marsha (1999). They also explained that corporate finance providers, including individuals, pension funds, mutual funds, banks, and other financial institutions, as well as governments, need guarantees that their investments will be safeguarded and yield profits. According to the Basel Committee (2015), protecting stakeholders' interests in accordance with the public interest on a long-term basis should be the main goal of corporate governance.

There are two possible meanings for the term "corporate governance": broad and narrow. In a narrow sense, it refers to the interaction between directors, shareholders, and business managers. It may also include how a company interacts with its stakeholders and the community. Even more broadly, "corporate governance" can refer to the set of laws, rules, listed regulations, and voluntary private sector practices that allow a corporation to draw in

capital, operate profitably, and satisfy both legal requirements and societal norms. Marsha and Holly (1999).

(Holly & Marsha, 1999) argues that corporate governance is crucial because countries all over the world are depending increasingly on the private sector to drive economic growth as markets become more open and global and business grows more complex. An increasing percentage of economic activity in both developed and emerging nations occurs in businesses.

To create goods and services that benefit society, corporations mobilize and integrate labor, capital, raw materials, management skills, and intellectual property from a range of sources. Consequently, efficient utilization of resources inside the company and the broader economy is encouraged by good corporate governance. By increasing the confidence of both domestic and foreign investors that assets will be used as agreed, good corporate governance helps businesses (and the economy) attract lower-cost investment capital. Lastly, companies must abide by the laws, rules, and expectations of the society in which they operate if they want to succeed in the long run.

Effective corporate governance is essential to the banking industry's and the economy's overall smooth operation, according to the Basel Committee (2015). By transferring money from savers and depositors to ventures that encourage business and propel economic expansion, banks play a vital role in the economy. Because banks' safety and soundness are essential to financial stability, how they operate is crucial to the health of the economy. Governance weaknesses at banks that play a significant role in the financial system can result in the transmission of problems across the banking sector and the economy as a whole.

Corporate fallouts can be limited to the stakeholders, but if a bank fails, the effects can quickly extend to other banks, potentially having major repercussions for the macroeconomy and the entire financial system (Kotnal, 2016). As a result, banks have different corporate governance than other businesses.

Corporate governance is defined by the Organization for Economic Co-operation and Development (OECD, G20/OECD Principles of Corporate Governance, 2015) as: *'Corporate governance involves a set of relationship between a company's management, its shareholders, and other stakeholders. Corporate governance also provides the structure*

through which the objectives of the company are set, and the means of attaining those objectives and monitoring performance are determined'

Additionally, the Basel Committee (2015) suggests that corporate governance establishes the authority and responsibilities by which a bank's board and senior management carry out its business and affairs. This includes how they:

- ❖ set the bank's strategy and objectives;
- ❖ choose and supervise employees;
- ❖ run the bank's operations on a daily basis;
- ❖ protect depositor interests, fulfill shareholder obligations, and consider the interests of other acknowledged stakeholders;
- ❖ align corporate culture, corporate activities, and behavior with the expectation that the bank will operate in a safe and sound manner, with integrity, and in accordance with applicable laws and regulations; and
- ❖ Establish control functions.

2.2. Corporate Governance in Ethiopia

The field of corporate governance research is very new, and its precise boundaries are still up for debate. Even while corporate governance aims to accomplish similar goals, its form varies depending on the jurisdiction. There isn't a pre-made corporate governance framework that nations may quickly adopt (Sefara, 2015).

In order to double its existing GDP by 2015 E.C., Ethiopia has started an ambitious Growth & Transformation Plan (GTP). Although these numbers show promise for the nation's economic development, both public and private investment are essential to achieving its goals. A strong regulatory framework and sound corporate governance are essential for economic development, which is a crucial precondition for eradicating poverty and generating wealth. (Tura, 2012).

The majority of Ethiopia's current legal codes, notably the 1960 commercial law, were "transplanted" from the continental European legal systems of the time, according to Sefara (2015). The general guidelines for corporate governance in Ethiopia are contained in this

code. The general norms of the commercial code were supplemented by other proclamations and directives. The three primary organs of management of share firms are acknowledged by the commercial code as being the board of directors, shareholders' meetings, and auditors. In Ethiopian share firms, shareholders are permitted to be members of the "one-tier" board of directors. The auditors are hired and given the responsibility of reviewing the financial records of share firms when shareholder meetings are held to adopt resolutions on significant issues pertaining to the companies. However, such clauses are insufficient to resolve certain board of directors-related corporate governance issues, such as the compensation of non-executive directors. This is according to Tura (2012).

Special rules of the same code or other independent proclamations and directives frequently supersede or supplement the regular company law regulations under the commercial code. In addition to the broad regulations outlined in the business code, financial share corporations are also subject to specific laws. Accordingly, banks and bank companies are governed under Banking Business Proclamation No.592/2008 and Bank Business Proclamation No.764/2012, respectively (Sefara, 2015).

In Ethiopia, commercial banks play a crucial role in the expansion of investment and capital formation. They encourage the public to deposit money and give consumers loans and advances. By taking part in the funding of public initiatives, they also aid in the nation's development. They purchase the government-issued bond for the Great Renaissance Dam's development. Additionally, Ethiopian commercial banks engage in a wide range of activities that fall under the umbrella of corporate social responsibility (Rao & Desta, 2016).

Therefore, it is crucial for Ethiopia that commercial banks operate effectively and perform well. The Ethiopian National Bank regulates them by issuing guidelines, taking into consideration their functions. In order to ensure the safety and soundness of the banking industry in particular and the financial system in general, NBE has issued new guidelines known as "Bank Corporate Governance Directives SBB/62/2015." Additionally, with the ultimate goals of achieving long-term shareholder value as well as the interests of consumers and other stakeholders, corporate governance promotes business prudence, prosperity, and accountability while allowing for balanced risk taking (NBE D. N., 2015).

2.3. Corporate Governance and the Nature of Banking Sector

Banks are essential to capital allocation, corporate governance, and industrial growth. There are consequences for business operations and national prosperity when private commercial banks operate well. The bank can increase its financial performance and distribute money more effectively if it designs and implements good corporate governance procedures. Additionally, shareholders' and other stakeholders' interests are safeguarded by efficient company governance (Levine, 2003).

On the other hand, if banks have inadequate corporate governance systems, they are less likely to deploy capital effectively. In this situation, the bank management will primarily take pleasure in working in his or her personal best interests rather than that of stakeholders or shareholders. This results in banking crises and collapses, which have severe repercussions and can have a substantial financial effect on the public (Levine, 2004). Effective corporate governance procedures are therefore necessary to establish and preserve public trust and confidence in the banking system, both of which are vital to the banking industry's and the economy's overall healthy operation.

Levine (2003) asserts that banks have two traits that are connected to their corporate governance. First, despite the fact that information asymmetries are present in all industries, they are more pronounced in the banking sector than in non-financial companies because of the opaqueness of their assets and operations. In the banking sector, loan quality can be concealed for extended periods of time. Furthermore, banks have the ability to alter the risk composition of their assets more quickly than the majority of non-financial sectors, and bank management can conceal issues by giving loans to customers who are unable to repay past debts. The agency problem is exacerbated by the increased information asymmetry between insiders and outsiders, as well as the comparatively significant challenges in gathering information about bank operations and keeping an eye on ongoing bank actions. Second, governments place strict regulations on banks, which are typically subject to strict oversight because of their significance to national economies.

The Basel Committee on Banking Supervision (2006) asserts that because of the financial intermediation function, corporate governance in the banking industry is more significant to the global financial system and benefits stakeholders and nations of banks in an economy, as well as the industry's high level of sensitivity to any problems brought on by poor corporate

governance and the requirement to protect depositors' money. The unique characteristics of banking necessitate both government intervention to curb the opportunistic behavior of bank management and a more comprehensive understanding of corporate governance, which includes the strategies used by lenders to control managers and guarantee that they receive a suitable return on their investment (Arun & Turner, 2004). Given the distinctive characteristics of banking institutions, if effective corporate governance is appropriately embraced and applied by the banks, it can benefit depositors as well as shareholders.

2.4.Theoretical Framework

2.4.1. Agency Theory

Agency theory, according to Habbash (2010), is a theory that is predicated on principal-agent connections. The framework for the operation of the agency theory is provided by the division of ownership and management in contemporary organizations. Modern organizations have widely distributed stockholders, or principals, who typically hire managers to run the business on their behalf rather than participating in day-to-day operations and management (Habbash, 2010). The agents are assigned to oversee the corporation's daily operations. However, if the agent acts to maximize their own worth rather than the principal's best interests, there may be a conflict of interest between the two parties. This kind of conflict arises because of differences in their preferred amount of managerial effort and risk tolerance, which can cause managers' and shareholders' objectives to diverge. Therefore, in order to solve the agency problem and/or align the interests of managers and shareholders, various control systems, either internal or external to the company, need be implemented.

A large portion of corporate governance, according to agency theory, is concerned with the boundaries of managers' accountability and discretion. The main criterion used by agency theorists to assess corporate performance is usually the maximization of shareholder wealth, and they inquire as to how the board might support corporate performance. Especially when the managers do not control the company's resources, the theory provides numerous helpful methods to analyze the connection between owners and managers and confirm how the ultimate goal of optimizing returns to the owners is accomplished. According to agency theory, corporate governance's monitoring mechanism helps resolve conflicts of interest between managers and owners and reduce agency or cost control. Evidently, the principal-

agent theory is typically regarded as the foundation for any discussion pertaining to corporate governance. It is anticipated that boards of directors will be autonomous, varied, and monitor as the owners' representatives, keep an eye on managers' behavior to make sure they are operating in the owners' best interests. According to the hypothesis, the makeup of the board plays a significant role in efficiently overseeing upper management. Boards must be gender balanced and diversified in terms of experience, education, and abilities. This maintains equilibrium on boards, results in efficient oversight, and ultimately contributes to the organization's successful operation. As a result, boards of directors are seen as a crucial tool for efficiently controlling managers and safeguarding shareholders from manager abuse.

2.4.2. Stakeholders Theory

Stakeholder theory is a development of agency theory, which holds that the board of directors should solely look out for the interests of shareholders. Stakeholder theory, on the other hand, broadens the agency theory's limited focus on shareholders' interests to include the interests of other persons and groups, such as interest groups pertaining to social, environmental, and ethical issues (Freeman et al. 2004).

Stakeholder theory is predicated on the idea that values are an explicit and necessary component of conducting business (Freeman et al., 2004). It invites managers to explain what unites its key stakeholders and how they all perceive the value they generate. Additionally, it encourages managers to be explicit about the types of business they wish to conduct of connections they must and desire to establish with their stakeholders in order to fulfill their mission. Stakeholder theory states that a company's goal is to serve and coordinate the interests of all of its stakeholders, including the government, the community, suppliers, consumers, shareholders, and employees.

Habbash (2010) defines a stakeholder as any individual whose objectives are directly or indirectly related to the firm, effected by the firm, or who has an effect on the accomplishment of the firm's objectives. These consist of the local community, government, political parties, staff, clients, suppliers, and management.

This idea states that the stakeholders in corporate governance have the ability to establish a positive external environment that supports the implementation of corporate social responsibility. A solid environment for long-term development can also be created by the

stakeholders in corporate governance, who will allow the business to think more about its consumers, the community, and social organizations. The advantage of the stakeholder model is its focus on addressing issues of underinvestment linked to opportunistic behavior and promoting proactive collaboration among stakeholders to guarantee the company's long-term prosperity (Maher & Andersson, 1999).

According to Kyereboah-Coleman (2007), management relies on staff to achieve the company's goal after receiving funding from shareholders. Customers, suppliers, and the community are examples of external stakeholders that are equally significant and subject to statutory and informal regulations that businesses must abide by. Stakeholder theory states that the most successful businesses have loyal suppliers, clients, staff, and management. Stakeholder theory has drawn more attention recently than it did in the past because scholars have realized that a company's actions affect the external environment and that it must answer to more than just its shareholders (Kyereboah-Coleman, 2007).

Businesses now function in society and are not only a tool for shareholders. It has obligations to the parties involved. Nonetheless, the majority of scholars contend that managers cannot realistically do this task (Sundaram & Inkpen, 2004b, Sanda et al. 2005). Not much empirical research has been done on the stakeholder theory. Stakeholder theory is frequently criticized for its inability to reconcile competing interests among stakeholders, which arises from the challenges of managing several stakeholders with disparate demands and wants. Treating every stakeholder equally is impossible (Habbash, 2010).

Furthermore, it is impractical to adequately represent all stakeholders in corporate governance suggestions since doing so could jeopardize the company's well-being (Habbash). According to Maher and Andersson (1999), the other criticism of the stakeholder model is that managers or directors could use stakeholder justifications to excuse subpar business performance.

2.4.3. Resource Dependency Theory

The book "The External Control of Organization: A Resource Dependency Perspective" by Jeffrey Pfeffer and Gerald Salancik raised public awareness of the "Resource Dependency Perspective" and helped it acquire traction in the Anglo-American discourse (Nienhuser, 2008).

Any organization's strategic management depends on the acquisition of external resources. All businesses rely on resources. Other businesses make up the resources that come from the environment (Abid, Khan, Rafiq, & Alia, 2014).

Organizations exchanged and transacted with other organizations, according to Pfeffer and Salancik (1978). The trades could include information, social legitimacy, or material or financial resources. Organizations are dependent on the environment for assistance because they are not self-sufficient. Businesses rely on one another and share resources since other businesses own the resources (Abid, Khan, Rafiq, & Alia, 2014).

Organizations' open-system character, which requires them to interact with environmental factors to acquire the resources they need to survive, leads to interdependence among them (Pfeffer & Salancik, 1978). Dependency can therefore be characterized as the result of the degree to which a particular input or output is controlled by a small number of organizations and the significance of that input or output to the organization.

Resources are the foundation of power for businesses since they are scarce, expensive to replicate, precious, and unreplaceable, claim Abid, Khan, Rafiq, and Alia (2014). Consequently, power and resources are closely related. When compared to their competitors who lack those resources, those businesses can be regarded as more strong.

Resource dependence theory's basic premise is that behaviors are influenced by "critical" and significant resources, which can be explained by the specific dependency situation (Nienhuser, 2008). External organizations may require certain actions from the organization in exchange for the organization continuing to offer what it requires (Pfeffer & Salancik, 1978). Therefore, if companies did not respond to the needs of their environments, they would not be able to survive.

According to the idea of dependence, organizations are somewhat guided by the factors in their surroundings and create their own plans of action in response to the requests made of them by other organizations. The demands and pressures of the organization and the groups in its surroundings affect and limit organizational behavior (Pfeffer & Salancik, 1978). Organizational uncertainty results from resource scarcity. Businesses constantly look for methods to take use of resources in order to secure their long-term existence (Abid, Khan, Rafiq, & Alia, 2014).

(Nienhuser, 2008) makes the case that having a clear understanding of which resources are essential is necessary to comprehend organizational behavior. Even if a given resource may only make up a very small portion of the overall resource needs or expenses, it is crucial if its absence jeopardizes the organization's capacity to operate. The actors and their relationship to the environment are the subject of resource dependence theory. There are several relationships of reliance because it is always about players who control resources and other actors who require these resources. It was supposed that performers wished to strengthen their power over others in order to lessen their reliance on them.

The fundamental tenet of resource dependency theory, according to Abid, Khan, Rafiq, and Alia (2014), is the necessity of environmental connections between the company and external resources. According to this viewpoint, the direction service uses the resources required for survival to link the company with outside influences.

Salancik and Pfeffer (1978) argue that when assessing one organization's dependence on another, three things are crucial. The first is the resources' significance, or how much the corporation needs them to stay in business and survive. The second is the degree of control the interest group has over the distribution and application of resources. The third is that the organization's reliance is mostly determined by how few options there are or how much influence the interest group has over the resource.

According to empirical data, resource dependence theory is a more effective lens for comprehending boards than agency, although being less frequently applied to board studies (Hilliman & Daiziel, 2003). Additionally, in 2014, Abid, Khan, Rafiq, and Alia also supports this as resource dependence theory underscores the importance of board as a resource and envisages a role beyond their traditional control responsibility considered from the agency theory perspective.

Given their opportunities to network and obtain information in different ways, resource dependency theory advocates for the nomination of directors to several boards (Abid, Khan, Rafiq, & Alia, 2014).

The resources board of directors performs two crucial roles for businesses, according to Hilliman & Daiziel (2003): it provides resources and oversees management on behalf of shareholders. According to proponents of resource dependence theory, board capital

determines how resources are provided. Consequently, this job directly relates to the board's capacity to provide resources to the company.

As a result, boards of directors play a crucial role in helping the company absorb essential aspects of environmental uncertainty. To overcome uncertainty, they connect the company with the outside resource. Because managing effectively with uncertainty is crucial for the existence of the company (Abid, Khan, Rafiq, & Alia, 2014).

The directors contribute information, skills, important constituencies (suppliers, purchasers, public policy decision makers, social groups), and legitimacy that would lessen uncertainty, in accordance with the resource dependency rule (Abid, Khan, Rafiq, & Alia, 2014).

(Daiziel and Hilliman, 2003) argues that boards should represent environmental requirements and be able to handle environmental dependencies. Additionally, they proposed four advantages that directors can offer the company: legitimacy, preferential access to resources, routes for information flow, and guidance and counsel.

The manager's job is to make decisions and legitimize them, according to Niehuser (2008). Managers make choices on how to manage internal actors and environmental requirements while also justifying those choices to stakeholders. In addition, he offers management techniques for managing resources and interacting with the environment:

- ❖ Adapting in the sense of organizational conformity, that is, satisfying the needs of a certain social actor,
- ❖ Preventing environmental influence,
- ❖ Controlling and preventing reliance, which includes developing substitute resources and controlling social control circumstances, which includes attempting to subjugate or lessen the power of controls.

In the same way, the board of directors is a tactic to reduce uncertainty. The size and makeup of the board of directors are influenced by resource dependency, according to Nienhuser (2008), who also contends that there is a connection between organizational structure and resource dependency because the more reliant an organization is on its resources, the more it can differentiate itself.

2.5. Empirical Review on Corporate Governance and Firm Performance and Hypothesis Development

This section of literature review concentrates on previous studies that have been conducted in relation to this study. There were mixed results concluded by previous studies pertaining to the relationship between corporate governance mechanisms and firms' financial performance. The important empirical studies are summarized below in this section.

Uadiale (2010) investigates how board composition affects Nigerian companies' financial results. He discovered that board size and company financial performance were strongly positively correlated. In order to determine if board structure affects financial performance as determined by return on equity and return on capital employed, it looks into the makeup of the boards of directors in Nigerian companies. Four board features—board composition, board size, board ownership, and CEO duality—have been recognized as potentially influencing corporate financial performance based on the substantial body of literature. These characteristics are used as the independent variables. The association between the independent variables and business performance metrics was estimated using Ordinary Least Squares (OLS) regression. He added that there is a favorable correlation between the financial performance of the company and the presence of outside directors on the board. However, there was a negative correlation found between the firm's financial success metrics and the directors' stockholding. Furthermore, the study finds that CEO duality and return on capital employed (ROE) have a negative relationship, whereas ROE and CEO duality have a strong positive relationship. According to the study, in order to improve corporate financial performance, a big board size should be promoted and the makeup of outside directors should be maintained and enhanced.

The effect of corporate governance on firm performance was studied by Ibrahim et al. (2010). They conducted a comparative examination of Pakistan's chemical and pharmaceutical industries utilizing a sample of five businesses from each industry between 2005 and 2009. Panel data approach and multiple linear regression models were applied. They employed three corporate governance factors—board size, board independence, and ownership concentration—and measured success using return on equity and return on assets. They discovered that whereas return on equity is significantly effected by corporate

governance in both sectors, return on assets is not much effected. According to industry study, corporate governance has a little effect on chemical and pharmaceutical companies' return on assets. whereas, in the chemical industry, corporate governance has a major effect on return on equity; whereas, in the pharmaceutical industry, the effect is insignificant.

A study on the relationship between audit committee characteristics and firm performance during the global financial crisis was carried out by Aldamen et al. (2011). Using a sample of 120 companies that were listed on the S&P 300 during 2008 and 2009, the researchers employed logit model analysis. Smaller audit committees with greater experience and financial knowledge are more likely to be linked to successful firm performance in the market, according to the study. Additionally, it was discovered that audit committee chairs with extended tenure have a detrimental effect on accounting performance. Nonetheless, audit committees with block holder representation, a chair with more years of managerial experience, and members with more external directorships have a good effect on accounting performance.

The relationship between corporate governance mechanisms and company performance was empirically investigated by Amran (2011). The effect of corporate governance practices on business performance was anticipated. 424 publicly traded Malaysian companies—233 family-controlled and 191 non-family-controlled—were used to test the hypothesis. Information regarding corporate governance practices and business success was gathered from the Sultanah Bahiyah Library database between 2003 and 2007. Tobin's Q was utilized as a gauge of business success, while board size, independence, director professional qualifications, leadership structure, debt, firm age, and firm size were used as corporate governance measures. The hypothesis was tested using panel data methods and the generalized least square estimation method. The sample was divided into two categories for the analysis: family-controlled and non-family-controlled firms. The study found that while director qualifications, as shown by the proportion of directors with a degree or higher divided by the total number of directors, improve the performance of non-family-controlled businesses, they have no effect on family-controlled businesses. The performance of family-controlled businesses was significantly effected negatively by board size and leadership duality, but this effect was negligible for non-family-controlled businesses. The performance of family-controlled and non-family-controlled firms was significantly correlated with

company age, both negatively and positively. controlled firms was significantly correlated negatively with firm size. For both groups of firms, the other factors, such the independence of the board and the professional qualifications of the directors, were negligible.

Al-Manaseer et al. (2012) used a total of 45 bank-year observations from 15 Jordanian banks listed on the Amman Stock Exchange between 2007 and 2009 to empirically examine the effect of corporate governance on performance. Pooled data and the OLS estimation method with panel methodology were used in the study. The study's dependent variables were return on equity, return on asset, profit margin (calculated by dividing net interest income by total asset), and earnings per share. Board size, independent board composition, the study's independent factors were banking size, foreign ownership, and executive officer position. The study identified a negligible negative correlation between board size and profit margin and return on assets, but a substantial negative correlation between board size and bank performance as shown by earnings per share and return on equity. Only the profit margin was significantly effected by bank size, which was adversely correlated with return on equity, return on assets, and profit margin. Additionally, the analysis shows that foreign ownership and bank performance are positively correlated with board composition. Chief executive officer status also has an adverse effect. The researchers conclude by proposing to prolong the study duration. When we see empirical evidence on banking sectors there is rare international evidence on corporate governance mechanism effect on performance in the bank industry compared to the literature on international corporate governance of typical public firms. One recent exception relates to the risk-taking behavior of European banking companies from the United Kingdom and Germany. Specifically, Eling and Marek (2011) are able to provide evidence that controls for the differences between the market-based U.K. corporate governance environment and the control-based system that prevails in Germany. Using a sample of 276 firms between 1997 and 2009, they proxy risk taking by asset risk and product risk, and focus on stock banking companies. Their corporate governance indicators include executive compensation, supervisory board compensation, and independence, as well as the number of board meetings and ownership structure. The study concludes that U.K. banking firms engage in more risk taking than their German counterparts and that large shareholdings and concentrated ownership contribute to increase interest risk taking.

To evaluate the relationship between corporate governance and risk-taking in terms of loan amounts, collateral claims, and interest rates, Lai and Lee (2011) take use of the unique organizational structure of the U.S. property and causality banking sector. The authors claim that the organizational structure of stocks may encourage risk-taking in order to boost shareholder wealth. In fact, stockholders with limited liability are more inclined to take chances in order to grow the value of the company and so reap the benefits of higher profits. In order to determine how to successfully reduce agency costs and create the right organizational structure, Najjar (2012) investigates how corporate governance practices affect the performance of Bahraini banking companies. Additionally, to differentiate between strong and weak corporate governance, which is an essential step in boosting market trust and drawing in beneficial investment flows for the organization and the economy. He concluded that there is no statistically significant influence of corporate governance, as measured by CEO status, ownership concentration, number of employees, industry performance, and number of shares traded, on the performance of the firm in the banking industry as measured by the dependent variable, return on equity (ROE), after applying the pooled data method to five commercial banks listed on the Bahrain Stock Exchange for the years 2005–2010. However, the dependent variable return on equity (ROE) indicates that the size of the board, the firm, and the number of block holders have a statistically significant effect on the firm's performance in the commercial banks sector. This outcome demonstrates how crucial a sound governance framework is for the company and the economy as a whole in the long run. To achieve the company's long-term objectives, foster stakeholder confidence, and produce favorable investment flows, the researcher advises that all banks should clearly define corporate governance and its procedures and execute them successfully.

Tornyeva et al. (2012) conduct research to look into the connection between Ghanaian banking businesses' financial performance and corporate governance. Both primary and secondary data were used; the former was gathered by administering interview questionnaires, while the latter was obtained from the national bank. The data analysis was conducted using the Panel Data Methodology. The results indicate that the financial performance of Ghanaian commercial banks is positively correlated with the following factors: dividend policy, annual general meeting, foreign ownership, institutional ownership, audit committee independence, long-serving CEOs, large board size, board skill, and

management skill. The authors contend that banks are urged to implement sound corporate governance procedures in order to enhance their financial results and safeguard shareholders' interests. To support the expansion and advancement of the banking sector, the regulatory bodies must, above all, enforce adherence to good governance and impose suitable penalties for noncompliance.

Jackson (2012) conducted research on the relationship between ownership structure, executive salary, and company performance for Chinese financial corporations between 2001 and 2009. The findings show that executive pay in Chinese banks is determined by a relationship-based contract rather than a market-based one. The pay-for-performance model of CEO salary in China is not well supported by data. While business size has a considerable favorable effect on CEO salary, ownership concentration has a significantly negative effect. Furthermore, while the compensation committee is cordial and raises manager salary, state ownership tends to restrict executive compensation. The findings imply that, in situations when corporate governance is lacking, the government or regulations may provide effective corporate governance in business operations.

Fadun (2013) looks at the opportunities and problems related to bank expansion and corporate governance. In addition to examining corporate governance theoretical perspectives, highlighting the difficulties of corporate governance in Nigeria, and investigating the connection between corporate governance and the expansion of banking companies in Nigeria, it promotes the necessity of sound corporate governance in the banking sector. The study's empirical design makes use of 112 respondents' survey replies and structured questionnaires. The Pearson product coefficient of correlation (r) is used to analyze data and evaluate hypotheses. The results show that prudent and safe banking practices are encouraged by effective corporate governance. Good corporate governance is encouraged by efficient supervision, and the new code of good corporate governance for Nigerian banks fosters the expansion of Nigerian banks. Effective corporate governance is required for banking organizations to operate properly in order to foster growth and maintain public trust, according to the practical implications. The study emphasizes how the Nigerian banking sector can produce more resources to support the economy through timely claims settlement and more job opportunities by implementing sound corporate governance principles.

A study on the effect of corporate governance on the financial performance of Kenyan listed commercial banks businesses was conducted by David et al. (2013). They specifically look at the effect of CEO duality, board composition, size, and debt on the financial performance of Kenyan listed commercial banks companies. Board size was found to have a negative effect on the financial performance of banks listed at the National Bank, and they use data from all those banks that were quoted on the Nairobi Securities Exchange as of December 2012 using a descriptive research design method. They also note that there is a strong correlation between the firm's financial performance and the corporate governance practices under study. Furthermore, they saw a favorable rapport between the board there are differences in composition and corporate financial performance. Regardless of whether the board members were executive or non-executive directors, the most important factor in board composition was their experience, expertise, and talents. Leverage has also been shown to improve the financial performance of banks that are listed on the Nigerian stock exchange. Regarding CEO duality, they discovered that the financial performance of Kenyan listed banks was positively effected by the separation of the CEO and chair roles.

2.5.1. Board Size and Firm Performance

The size of the board may have an effect on its efficacy; claim Rao and Desta (2016). There are arguments for both smaller and larger boards to be effective in regulating managers because there is now no clear consensus on the size of the board.

There is a claim that larger boards of directors are more successful at monitoring and advising management because they attract more human capital. One criticism, though, is that when a board grows too large, it becomes challenging to manage, promotes free riding, and causes issues. Thus, small boards may boost individual director accountability and decrease the likelihood of free riding (Rao & Desta, 2016).

In light of this, some research (Al-Sahafi, Rodrigs, & Barnes, 2015) and others (Grove, Patelli, & Victoravich, 2011) suggest that larger boards resulted in improved performance. According to research from Saudi Arabia, board size and board independence are positively correlated with ROA at the 5% and 10% significance levels, respectively (Al-Sahafi, Rodrigs, & Barnes, 2015). This suggests that as the board grows larger and more autonomous, ROA rises. Additionally, at the 1% level of significance, the ROE model

showed a strong positive correlation between board size and ROE. This implies that a larger board increases the likelihood of improved bank performance.

As a result, they advise the bank to have a large board (nine to eleven members) since it improves financial success.

A research of US commercial banks revealed that board size has an inverted U-shaped or concave relationship with bank performance (Grove, Patelli, & Victoravich, 2011).

This suggests that while a larger board is linked to better financial results, performance will suffer if the board grows too big.

On the other hand, other research as well (Ranti & Samuel, 2012; Naushad & Malik, 2015; Manini & Abdillahi, 2015; Khan, Malik, & Umbreen, 2017; Zabri, Ahimed, & Wah, 2016) show that smaller boards result in greater performance. Samuel and Ranti (2012), reveals a negative correlation between Nigerian banks' financial performance and board size. This suggests that because agency problems increase with board size, larger boards are less effective than smaller ones. This leads decision-making power of the board to become slower with the involvements of more people. Thus they conclude that the large board size leads to the free rider problem where most of the board members play a passive role in monitoring the firm. Moreover, the board members tend to become involved in dysfunctional conflicts where the board is not cohesive (board members are not working optimally to achieve a single goal) deteriorating the value of the firm.

There are also studies that argues board size doesn't have an effect on the financial performance of banks such as (Rao & Desta, 2016) and (Abdul-Quadir & Kwanbo, 2012)

Therefore the previous empirical results are inconclusive on the relationship between board size and financial performance. Thus the hypothesis is stated as:

H₀₁: Board Size Has Negative Effect on the Financial Performance of Commercial Banks in Ethiopia.

2.5.2. Frequency of Board Meeting and Firm Performance

The majority of corporate governance literature focused primarily on board size or composition as a gauge of participation in overseeing management, ignoring other aspects of board oversight such board meetings (Akpan, 2015).

The NBE's Bank Corporate Governance Directives No. SBB/62/2015 regulation on corporate governance mandates that banks hold frequent board meetings in order to carry out their obligations. "A board meeting shall be held at least once in a month on the date and at the venue fixed in accordance with the rules for manner of conducting the board meeting," the instruction reads. Additionally, note that at least 75% of the board meetings of the bank should be attended in person by the board members within a financial year.

Since the beginning of time, the biggest obstacle facing humans on our planet has been the unsolvable issue of risks and uncertainties. Despite the tremendous advancements in science and technology that we have seen over the years, this issue has not been overcome. The human mind's most creative solution to this risk issue, as seen from a societal and economic perspective was commercial banks. An important factor in economic growth is commercial banks. Through commercial banks savings that are converted to investments, it helps the economy's asset base expand (Swiss Re 2011). Establishing strong corporate governance in the commercial banks industry is essential to achieving the aforementioned advantages.

According to Akpan (2015), the board needs to convene on a frequent basis in order to carry out its oversight role and keep an eye on management performance. There are conflicting empirical findings regarding the relationship between regular board meetings and company performance.

According to research findings like those of Ntim and Osei (2011), who studied 169 South African listed companies between 2002 and 2007, there is a statistically significant and positive correlation between corporate board meeting frequency and corporate performance. This suggests that boards in South Africa that meet more frequently tend to produce better financial results. This finding lends factual credence to the agency hypothesis, which contends that more frequent meetings of corporate boards enhance their ability to counsel, oversee, and discipline management, thus enhancing the financial performance of the company.

However, the findings of studies like (Johl, Kaur, & Cooper, 2015), (Taghizadeh & Saremi, 2013), and (Akpan, 2015) indicate that board meetings have a negative and substantial relationship with the performance of the company. According to a study by Johl, Kaur, and Cooper (2015), which looked at 700 publicly traded companies in Malaysia in 2009, the average number of board meetings per year is five, with a range of 0 to 24. Because of their line of work, the banking and financial industries typically hold board meetings on a much more frequent basis. Additionally, they discovered a substantial and negative correlation, at the 5% level, between the frequency of board meetings and company success, suggesting that The success of the company is negatively effected by the frequency of board meetings since too many meetings may cause resources to be diverted to less fruitful endeavors.

Saremi and Taghizadeh (2013) Board meeting frequency was found to have a negative and significant connection with ROE and ROA at the 1% and 5% levels of significance, respectively suggests that a high board meeting frequency lowers ROE and ROA levels. 150 Malaysian companies that are publicly listed make up the study's sample.

Similar findings are found in another study by Akpan (2015), which examined 79 businesses listed between 2010 and 2012 on the Nigerian Stock Exchange and discovered a substantial negative correlation between board meetings and company performance. As a result of the corporation incurring higher costs for sitting allowances, travel, hotel accommodations, and entertainment during meetings, the frequency of meetings decreased shareholder earnings.

Based on the aforementioned considerations, this study aims to resolve the conflicting results regarding the frequency of board meetings with business performance. Consequently, the following theory is established:

Ho2: There Is No Relationship between the Frequency of Board Meetings and Financial Performance of Commercial Banks in Ethiopia.

2.5.3. Board Gender Diversity

Board diversity, according to Enobakhare (2010), is the combination of males and women, individuals from various age groups, and individuals from various racial and ethnic origins. Gender diversity, or the presence of women on corporate boards of directors, is a contentious

issue that is seen as a way to increase board diversity and, consequently, conversations. It is calculated as the total number of female board members for a given time period. The integrity of the company's finances is one of the duties of the board of directors, according to the OECD's 2004 principles of corporate governance. The presence of suitable control systems, specifically those for risk management, financial and operational control, and adherence to applicable regulations and standards, as well as accounting and financial reporting systems, including the independent audit. Gender diversity in the board's makeup is necessary for them to carry out their duties.

Boards are concerned with being properly constituted to offer a range of viewpoints. According to Boyle and Jane (2011), having women on boards offers certain extra views and abilities that would not be available on all-male boards. A more diverse board might make it harder for the management to sway it in favor of their own agenda. Effectiveness in the supervisory role of boards of directors is linked to gender diversity, which could be more effective if there is gender diversity on board.

Various theoretical stances favor gender diversity on the boards. The monitoring role of directors is the primary focus of agency theory, which also emphasizes that a balanced board would result from representation from a variety of groups, preventing any one person or group of people from controlling the board's decision-making (Erhardt et al., 2003). The stakeholders' approach states that diversity also ensures equity and fairness by representing the firm's various stakeholders (Keasey et al., 1997). According to Walt and Ingley (2003), the board is a strategic resource that serves as a link to a number of external resources. Diversity on the board facilitates all of these.

However, Rose (2007) found no correlation between the number of female directors on the board and the performance of the company. But a lot of academics now think that more diversity on boards improves governance since it enables boards to access a wider range of talent for director positions (Bathula, 2008). Additionally, Belete Zegeye (2015) discovered that the gender makeup of the board has no discernible effect on the microfinance institutions' financial performance.

Research has shown no correlation between financial performance and the gender diversity of the board. For instance, (Rao & Desta, 2016) found no statistically significant correlation

between bank financial success as evaluated by ROA and ROE and board gender diversity. This suggests that the financial performance of banks is not statistically effected by the increased percentage of female directors in the boardroom. The findings of a study conducted on 42 Kenyan banks as of December 31, 2014, revealed a statistically insignificant correlation between board gender diversity and bank financial performance (Manini & Abdillahi, 2015). As a result, the idea that gender diversity improves a bank's financial performance is not supported by this data. (Appiah and Agyapong, 2015) Additionally, Shafique, Idress, and Yousaf (2014) found no statistically significant correlation between the proportion of women on board and the financial success of Ghanaian public companies as determined by ROA and Tobin's Q.

As a result, the prior empirical findings about the connection between board gender diversity and financial performance are not conclusive. The hypothesis is so expressed as follows:

Ho3: Board Gender Diversity Has No Effect on the Financial Performance of Commercial Banks in Ethiopia

2.5.4. Educational Qualification of Directors

The term "educational qualification" describes each board member's level of competence. When making decisions, each board member's qualifications are crucial. Higher qualified board members aid the companies by contributing a variety of skills and abilities that foster a range of viewpoints in decision-making. More qualified members would broaden the board's knowledge base, encourage members to think of various options, and improve more deliberate problem-solving. The percentage of board members with at least a college degree relative to the total number of board members serves as a gauge. In organizational environments, having more educated directors is positively correlated with being more open to innovation, being more creative, and making better strategic decisions. The educational background of the director is essential for properly interpreting and using the data generated by the management.

Since the capacity to locate and analyze relevant information is necessary for the smooth running of a contemporary organization and for boards of directors to effectively control or guide management, educational background is significant. Boards of directors' oversight and

monitoring functions are effected (Gantenbein and Volonte, 2011). Given that the corporate board is one of the mechanisms for monitoring the company and may be able to supply the expertise required to operate in the new environment, the human capital offered by its board of directors is crucial. According to Poon, Heong, and Lee (2013), there is a favorable correlation between directors' qualifications and performance. Their findings lend credence to the idea that company performance is enhanced by senior management teams with backgrounds in business-related fields including banking, auditing, law, accounting, business administration, information technology, investment management, or finance. These capable directors made the decision to improve company performance in order to enhance the company's reputation and show responsibility and authority among the management group.

The effectiveness of the board depends on the personal characteristics of the directors, such as their training and experience. Therefore, directors with business qualifications may be more effective than those with less training (Ferreira, 2010). As a result, the prior empirical findings about the connection between directors' educational background and financial performance are not conclusive. The hypothesis is so expressed as follows:

Ho4: Directors' educational qualification has positive Effect on the Financial Performance of Commercial Banks in Ethiopia

2.5.5. Board Experience in the Finance Sector

Board members with employment expertise in the finance industry are referred to as having board experience. According to Ayalew (2007), most bank board members in Ethiopia lack awareness and, as a result, do not implement best practices in corporate governance within their banking sector.

The quality of information gathered, problem-solving, opinions held, and decisions made during the decision-making process will all be improved by assigning directors with relevant and related skills and knowledge to carry out task-specific responsibilities like the company's internal control and procedures (DeZoort, 1998 as cited by Saat et al 2011). According to their research, directors with experience are better able to control, steer, and oversee the company. In other words, their knowledge of the industry, its opportunities and threats and their connections to the industry participants based on their experience enables them to contribute substantively in the firm performance. Moreover, Ferede (2012) found that a

positive association is found between industry specific experience and return on asset and return on equity in Ethiopian Banking Industry. Thus the hypothesis is stated as:

Ho5: Directors' experience in finance sector has positive Effect on the Financial Performance of Commercial Banks in Ethiopia

2.5.6. Chief Executive Compensation.

Although some academics contend that a positive relationship is either not well-established or only weakly supported, the agency-based theory generally supports the idea that executive compensation and firm performance are positively correlated (Haid and Yurtoglu, 2006; Nourayi and Mintz, 2008; and Lazarides et al., 2008). Fernandes (2005), for example, uses data from the Portuguese Stock Exchange to infer that CEO compensation is not much effected by firm success. He also asserts that there is no correlation between executive income and stockholder wealth. According to more recent research by Jeppson et al. (2009), CEO pay is positively correlated with a company's overall revenue but unrelated to changes in net income or total shareholders' return. In conclusion, varied data, institutions, and model specifications result in distinct pay-for-performance settings. In contrast, emerging nations have not conducted a thorough analysis of CEO equity incentives and executive compensation (Kato and Long, 2006). Furthermore, less is known about the compensation of Chinese CEOs in comparison to those in Western nations. In accordance with conventional thinking, this study postulates that:

H6: There is no significant relationship between chief executive's compensation and banks' financial performance in Ethiopian.

2.6. Summary and Research Gaps

Regardless of an organization's size, growth, or industry, corporate governance is crucial. The institution in question benefits economically from good corporate governance since it protects the company against losses brought on by corruption, fraud, and other irregularities. Additionally, it encourages entrepreneurial innovation, which helps the company better take advantage of any financial opportunities that present itself. The primary principles of corporate governance that are currently being addressed include ensuring that management and the board are sufficiently separated to allow the board to direct and oversee management,

as well as separating the chairman and chief executive positions to ensure that the board has a good balance of independent and non-independent directors and establishing the independence of the auditor and, consequently, the integrity of financial reporting, including the creation of a board audit committee. Increased profitability and efficiency of businesses, as well as their improved capacity to generate money for shareholders, more job possibilities with better terms for employees, and benefits for stakeholders, are the goals of good corporate governance.

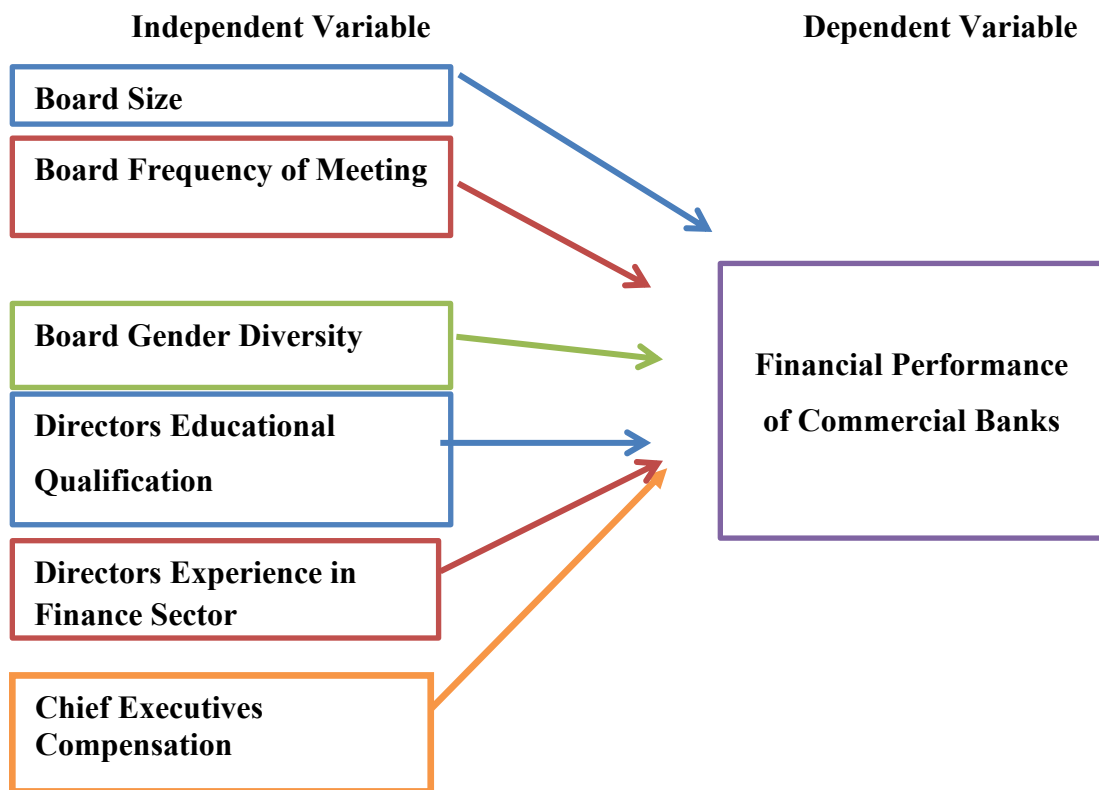
Therefore, ensuring corporate efficiency, resolving conflicts, ensuring transparency and legitimacy of corporate activity, reducing investment risk and yielding high returns for investors, and providing a framework for managerial accountability are the primary responsibilities of corporate governance.

The majority of the studies referenced in the literature focus on industrialized nations with corporate governance structures and strategic approaches that differ from Ethiopia's. There aren't many studies on corporate governance topics conducted in Ethiopia. For example, Minga (2008) examined the legal and other external institutional frameworks of corporate governance in Ethiopia and came to the conclusion that the nation's overall corporate governance standards were lacking. Fekadu (2010) also examined Ethiopia's corporate ownership structure and found that, although the Commercial Code's ability to safeguard the rights of minority shareholders is lacking, the country's division between ownership and control—that is, between shareholders and management—is widening. Furthermore, Ahemad (2012) examined Ethiopian company law and discovered that it lacked sufficient legislative provisions on governance matters pertaining to the division of management and supervision duties as well as the independence, composition, and compensation of the board of directors in share companies. More precisely, an unpublished master's thesis or research paper on Ethiopia's banking industry was submitted. Ferede (2012) studied to find out how corporate governance works and how it affects Ethiopian commercial banks' performance.

Prior research, which tended to focus on wealthy nations, has generally made significant contributions to corporate governance and financial success. However, the majority of the literature on this topic focused on the banking sector, with developing nations receiving minimal attention. As a result, a design element that is effective in one nation or sector could

not be in another. According to Bird (2005), this may be called the No-One-Size-Fits-All (NOSFA) principle, which states that the optimal administrative structure and policy for any nation or business must be carefully chosen based on its unique goals and circumstances.

Despite the growing volume of research examining the relationship between corporate governance and firm performance, existing studies present several limitations that constrain their generalizability and practical relevance—particularly within the context of developing economies. First, much of the prior literature has been concentrated in developed countries with mature financial markets, strong regulatory enforcement, and well-established corporate governance frameworks. Consequently, findings from these environments may not be directly applicable to countries like Ethiopia, where institutional structures, governance practices, and financial systems are still evolving. Second, earlier studies have predominantly focused on manufacturing, commercial banks, or non-financial firms, leaving a critical gap in the understanding of governance dynamics within commercial banks, which operate under distinct regulatory and risk environments. Third, many of these studies employed cross-sectional or short-term data, limiting their ability to capture long-term governance effects on performance. Additionally, most research relied solely on quantitative methods, overlooking valuable insights that could be gained through qualitative engagement with board-level decision-makers. In the Ethiopian context, the few available studies tend to emphasize legal frameworks or general ownership structures, rather than examining the nuanced, internal governance variables such as board qualifications, gender diversity, and CEO compensation. These limitations collectively underscore the need for a comprehensive, mixed-method, and context-specific investigation—an area this study seeks to address.



Source: Adapted and Modified from Rasheed and Awan (2021) and Literature Review

Figure 2.1: Conceptual Framework of the Study

CHAPTER THREE

RESEARCH METHODOLOGY

The methodologies that were employed for the study are presented in this chapter. It clarifies the research strategy. Information was provided regarding the demographic, sample, sampling methodology, research tools used in the study, data collection procedures, and a strategy for data analysis.

3.1. Research Design

According to Creswell (2003, p.13), there are three typical approaches to business and social research in terms of investigative study: mixed methods, quantitative, and qualitative. By analyzing the relationship between variables, quantitative research can be used to test objective ideas (Creswell 2009). Conversely, a qualitative research approach aims to inductively construct a theory or pattern by investigating and comprehending the meaning that people or groups assign to a social or human situation (Creswell 2009).

The last strategy is the mixed methodologies approach, where researchers focus on the study problem and employ every strategy at their disposal to comprehend it (Creswell, 2003).

Given the foregoing descriptions of mixed, qualitative, and quantitative research methods, the quantitative method is typically employed in this study. However, the qualitative method of inquiry is used in addition to the quantitative method to obtain a deeper understanding of the research problem. In other words, the current study integrates both quantitative and qualitative research procedures in order to achieve the advantages of a mixed methods approach, as previously mentioned, and to reduce the bias associated with using only one of

the two ways. The description of the research methodology employed in this study is the main topic of the next section.

3.2. Research Approach Adopted

The research method employed in a study informs decisions on the type of data gathered, the research instrument chosen, and the data analysis. Because it determines the caliber of study findings, choosing the right research procedures is crucial. The effect of corporate governance mechanisms on the financial performance of banks in Ethiopia has been best studied using a hybrid approach, which encourages the combination of both qualitative and quantitative data. The main idea is that combining quantitative and qualitative methods improves knowledge of study issues compared to using just one method (Creswell 2009). As a result, the quantitative and qualitative components of the research methodology are covered in turn in the sections that follow. The mixed research approach is selected because it enabled the researcher to examine both the statistical relationships between corporate governance variables and financial performance and to explore the contextual understanding behind governance practices in Ethiopia's commercial banking sector.

3.2.1. Quantitative Aspect of Research Method

The quantitative research approach uses statistical analyses and numerical data to address concerns regarding the correlations between the variables being assessed. This study adopted a survey design since it is economical and allows for the collection of sufficient data, even if there are two strategies of inquiry under the quantitative method. This study also aims to investigate how corporate governance affects Ethiopian banks' financial performance. The link between the independent and dependent variables needs to be described quantitatively or numerically.

As a quantitative research method, the survey can gather quantitative data in a variety of ways. According to Creswell (2009, p. 146), Fink (2002) states that there are four methods of gathering data: surveys, self-administered questionnaires, interviews, structured record reviews to collect financial, medical, or school information and structured observations. The survey instrument adopted in this study to collect data was a structured record review. The following section, accordingly, reviews the issues in a sample design in respect of the current study.

Sample Design

The National Bank of Ethiopia serves as the nation's central bank and is part of Ethiopia's financial system. 29 banks that operate in Ethiopia make up the study's total population (NBE, 2023). This analysis takes into account the five-year period from 2019 to 2023.

Purposive sampling is the sample technique employed. As a result, samples are chosen from the population using three criteria. The bank must first engage in commercial banking operations under the direction of the board of directors. One state-owned bank was disqualified from this study based on this criterion. This bank serves as Ethiopia's development bank. By raising money from both domestic and foreign sources and guaranteeing its sustainability, this specialized financial institution was founded to advance the national development agenda by providing development finance and close technical assistance to feasible projects from the government's priority areas (Rao & Desta, 2016). Second, a commercial bank ought to be in business for ten years or more (Ensure stability, maturity in board governance practices and to allow a robust five-year performance trend analysis).

Exclude newly established banks that may not have fully developed governance frameworks or sufficient financial history. The third criterion is having a comparatively higher level of capital (This threshold was derived based on: The minimum capital requirements set by the National Bank of Ethiopia (NBE) for commercial banks, which has been incrementally increased over time and the researcher needed to include banks with significant market share, broad customer bases, and more institutionalized governance structures), and the fourth is data availability. By applying these benchmarks, the study focuses on commercial banks that have both governance maturity and capital adequacy, allowing for meaningful evaluation of how internal corporate governance mechanisms relate to sustained financial performance in Ethiopia's banking sector. To this respect, one bank is excluded from the study because, as a result of the merger of Ethiopia's commercial and business banks, there is no separate annual report for construction and business banks during the study period. Accordingly, 5 commercial banks met these criteria and they are considered for the study.

Table 3.1: Sample Size

No.	Name of the Commercial Bank	Year of Establishment in G.C.	Capital in ETB
1	Commercial Bank of Ethiopia	1942	1.3 Trillion
2	Awash Bank	1994	27.968 billion
3	Bank of Abyssinia	1996	19.475 billion
4	Dashen Bank	1995	19.319 billion
5	Cooperative Bank of Oromia	2005	14.874 billion

Source: NBE, (2023)

3.2.2. Qualitative Aspect of the Study

A method for investigating and comprehending how people or groups respond to a social or human issue is the qualitative research technique (Creswell, 2009). In qualitative research, questions about complex phenomena are usually addressed through the use of instruments such as unstructured interviews, group discussions, field notes for unstructured observation and reflection, various texts such as reflexive journals, photographs, and document and literature analysis. Therefore, in-depth interviews were conducted in the current study to collect the qualitative data required to further address the aims described in the previous section.

In-depth Interviews

Selected board chairs from the sample of banks were interviewed in-depth. Since they are thought to be the most knowledgeable about the topic being studied, three board chairs and one designated individual are specifically taken into consideration for discussion in this study. The people who are regarded as board chairman are highly knowledgeable and competent in their respective fields. In order to obtain further information, the researcher generally asked a series of unstructured interview questions depending on the goal stated in the section before this one.

An interview was appropriate to gather information since the nature of this study necessitates a thorough comprehension of the effects of corporate governance mechanisms on the financial performance of bank businesses in Ethiopia. According to Easterby-Smith et al. (1991), the interview method is the most basic of all qualitative techniques and is thought to be the most effective way to collect data.

An in-depth, unstructured, in-person interview was done by the researcher. Because of its adaptability and ability to accommodate new topics throughout the interview, the unstructured face-to-face interview was chosen as the instrument.

The non-probability purposive sampling approach was used for the sample design. Therefore, three board chairmen and one designated individual were interviewed utilizing unstructured face-to-face interviews at various times in order to investigate the topic of corporate governance mechanisms.

3.3.Method of Data Analysis

Descriptive statistics, correlation, and multiple panel linear regression techniques have been used to examine the data gathered utilizing the aforementioned instruments. The mean, maximum, minimum, and standard deviations of the variables have been employed in descriptive statistics to quantitatively characterize their key attributes. The association between the variables has been determined using Pearson correlation analysis. However, it prevents the researcher from drawing conclusions about the causal link between variables (Marczyk et al., 2005). In order to test the hypothesis and explain the association between corporate governance variables and financial performance metrics by controlling the influence of selected variables, a multiple panel linear regression analysis was also employed. The qualitative information gathered via questionnaires was subjected to

qualitative analysis. The SPSS 23 software package is used to do the least squares analysis, and the results are displayed in tables and figures.

The variables were chosen using prior empirical research on corporate governance and business performance as well as alternative theories such as agency and stakeholder theories. In order to investigate the effect of corporate governance procedures on the financial performance of private commercial banks, the independent, dependent, and control variables of the study were determined based on the theory and empirical research.

3.4. Study Variables

The association between corporate governance practices and Ethiopian commercial banks' financial performance was examined using a quantitative research methodology. The following describes the specifics of how the variables are measured and applied in the research. The study takes into account the independent, dependent, and control factors.

Dependent variables: Accounting-based metrics are employed to assess the commercial bank's financial performance. Return on asset is this metric. In earlier research, such accounting measures were commonly employed. The body of current literature served as the basis for the selection of these metrics. Rao and Desta (2016), Naushad and Malik (2015), Manini and Abdillahi (2015), Ajanthan, Balaputhiran, and Nimalathashan (2013), Zabri, Ahimed, and Wah (2016), and Al-Sahafi, Rodrigs, and Barness (2015), for example, all employed accounting metrics.

Returns on assets (ROA) show the profitability of the company's assets in generating profits. In other words, it indicates the effectiveness of the firm's assets in increasing shareholders economic interests. It also shows the efficiency of management in using its asset to generate earnings (Rao & Desta, 2016). ROA is calculated as follows.

$$ROA = \frac{\text{PROFIT AFTER TAX}}{\text{TOTAL ASSET}}$$

Independent Variables: The following are the independent variables of the study and the selection of each of the variables is backed by empirical evidence.

Board Size – (BZ): The total number of directors in the board sampled commercial banks in Ethiopia.

Frequency of Board Meeting (FBM): The total number of board meeting conducted per year of sampled commercial banks in Ethiopia.

Board Gender Diversity (BGD): The ratio of the number of female directors to board size of sampled commercial banks in Ethiopia.

Directors' Educational Qualifications (DEQ): Number of directors who had college degree or higher.

Directors' Industry Specific Experience (DISE): Number of directors who served in other bank sector earlier in the same capacity.

Chief executives' compensation (CEC): Natural log. of chief executives composition in amount birr.

3.5. Model Specification

In 2016, Rao and Desta As stated in Himmelberg, Hubbard & Palia (1999) contend that a large number of earlier cross-sectional research do not account for unobserved firm heterogeneity, which could lead to erroneous relationships. Therefore, using a panel technique enables greater control for endogeneity issues and time-invariant firm effects. Furthermore, (Rao & Desta, 2016) propose that panel data analysis reduces multi-collinearity among variables and eliminates unobservable variability for each observation in the sample. Therefore, in order to quantify the effect of corporate governance variables on the financial performance of Ethiopian commercial banks, a panel regression model was used in this study. This approach was used by (Fatimoh, 2012), (Manini & Abdillahi, 2015) and (Rao & Desta, 2016) the following general empirical research model is developed.

$$Y_{it} = \beta_0 + \beta_1 Git + \beta_2 Cit + \epsilon_{it}$$

Where,

Y_{it}: represents financial performance of banks at time t.

β₀: is the intercept: is a vector of corporate governance variables.

Git: is a vector of corporate governance variables.

Cit: Control variables.

ϵ_{it} : the error term which account for other possible factors that could influence Y that are not captured in the model.

The above general empirical research model is changed in to the study variables to find out the effect of corporate governance mechanism on firm financial performance as follows:

$$ROA_{it} = \beta_0 + \beta_1 BZ_{it} + \beta_2 FBM_{it} + \beta_3 BGD + \beta_4 DEQ + \beta_5 DISE + \beta_6 CEC + \epsilon_{it}$$

Where,

i = denote banks ranging from 1 to 5 (Cross-sectional dimension).

t = denote years ranging from 2019-2023 (Time-series dimension).

ROA = Return on Asset for i^{th} bank and time period t

BZ = Board Size for i^{th} bank and time period t

FBM = Frequency of Board Meeting for i^{th} bank and time period t

BGD = Board Gender Diversity for i^{th} bank and time period t

DEQ = Directors Educational Qualification for i^{th} bank and time period t

DISE = Directors Industry Specific Experience i^{th} bank and time period t

CEC = Chief Executives Compensation i^{th} bank and time period t

CHAPTER FOUR

DATA ANALYSIS AND PRESENTATION

This chapter presents the results of the investigation by the researcher based on the methodology stated in chapter three. It includes the general background of the respondents and detailed discussion of the six specific objectives and analysis of descriptive statistics through IBM SPSS version 21. Before running any analysis tests were carried out in order to test whether the results were reliable, or internal consistency of the overall factors were checked through Cronbach alpha and also the validity was tested using the content validity. The findings of the study were also discussed in a relation to the literature review.

4.1. Descriptive Statistics Analysis of Regression Variables

Table 4.1 provides a summary of the descriptive statistics of the dependent and independent variables for five commercial banks for a period of five years from year 2019-2023. The table includes the mean and standard deviation for the independent and dependent variables of the model. This was generated to give overall description about data used in the model and served as data screening tool to spot unreasonable figure.

As shown in chapter three, return on asset which gives an idea how efficient management is at using its assets to generate earnings was measured as net income after tax divided by total asset. The average value of return on asset for the sample Ethiopia commercial banks is 13 percent (mean=0.13) with a standard deviation value of 0.11. This result indicates that most performing commercial banks among the sampled banks earned 13 cents of profit after tax for a single birr invested in the assets of the firm. The result implies that these Insurers need to optimize the use of their assets to increase the return on their assets.

Table4.1: Descriptive Analysis of Regression Variables

Variables	Mean	Median	Maximum	Minimum	Std. Dev.	Observations
ROA	0.13	0.10	0.37	-0.05	0.11	100
BZ	10.12	10.00	12.00	7.00	1.49	100
FBM	6.81	6.50	14.00	4.00	2.76	100
BGD	0.86	1.00	4.00	0.00	1.10	100
DEQ	6.31	6.00	9.00	2.00	2.14	100
DISE	2.93	3.00	6.00	1.00	1.49	100
CEC	5.52	5.55	6.19	4.70	0.35	100

Source: Researcher's Own Survey Findings (2025)

Regarding explanatory variable there are some imperative statistics that have to be mentioned. Board size of sample commercial banks which is measured as number of directors set on board. It is confirmed in the table below that the average board size for the sample commercial banks is about 10 members (mean = 10.123), with maximum board members of 12 and minimum board members of 7. In Ethiopian context, board size generally complies with NBE's minimum requirement (9 members). Studies show mixed effect, too small lack oversight, too large lacks cohesion (Admasu, 2017). The standard deviation indicates that for the sampled commercial banks' board size (0.71) indicates that there is low dispersion in the board size of the sample banks during study period.

Furthermore, another interesting observation is that there was somewhat a higher variation in frequency of board meeting during study period which is measured as Number of directors meeting in the year, maximum of 14 times, minimum of 4 times and on average is 6.81. Generally the sample commercial bank conduct meeting 6.81 or 7 times on the average which is high when we compare with currently proposed corporate governance guidelines by

National Bank of Ethiopia for banks which postulates as each bank should at least conduct meeting of 4 times in a year. Frequency of board meeting implies active governance and responsiveness. Fikru (2021) finds a positive but diminishing returns beyond certain point, suggesting that quality of meetings may matter more than quantity.

With regard to Board Gender Diversity, which is measured as number of female directors who seat in board as directors, table 4.1 indicates that the mean and standard deviation of female directors in the board of the selected commercial banks to be 0.86 and 0.73, respectively. The result suggests that there are small number and high dispersion of women in the board during the sample period. Gender diversity improves decision making quality through diverse perspectives. However, female representation in Ethiopian commercial banks still remains low.

Furthermore, educational qualified directors measured as number of directors who had college degree or higher had maximum value of 9, minimum value of 2 and mean value of 6.31 or 6 directors which indicates on average directors who have collage degree or above was 8 people during study period sample commercial banks. This implies that from selected commercial banks, high educational attainment among board members boosts financial literacy, enhancing strategy formulation and risk oversight. As highlighted by Mahilet (2021), this variable has strong correlation with bank financial performance.

The table 4.1 above also depicted Directors' Industry Specific Experience, which was measured as number of directors who served in other banks earlier in the same capacity and the descriptive statics shows as the mean value of directors in the boards of selected commercial banks who have prior experience in banking sectors had maximum value of 6, minimum value of 1 and mean value of 2.93 or 3 directors. This also suggests that only small number of directors in Ethiopian banking industry have specifically prior bank related experience. Board members with relevant experience can better anticipate industry risks and trends. Studies in local context affirm that experience significantly affects performance by improving the quality of decisions (Mahilet, 2021).

Finally, the table 4.1 above reveals that the mean value of chief executive officer compensation of the selected commercial banks had maximum value of 6.19, minimum vvalue of 4.7 and mean value of 5.52 during a study period which was measured by the

natural logarithm of chief Executives' payment. CEO pay structures are intended to align the CEO's incentives with shareholder wealth. Ethiopian studies are limited, but those like Getachew (2017), suggests compensation correlations positively with performance up to a point.

4.2. Results of Inferential Statistics

In this part, the inferential statistics findings were displayed. Pearson's Correlation Coefficient and Multiple Regression Analyses were conducted in order to achieve the study's goals. Conclusions and decisions about the research hypothesis were generated with the use of these statistical approaches.

4.2.1. Pearson Correlation Analysis

The strength of a linear relationship between two variables can be assessed statistically using correlation analysis. According to Table 4.2's correlation results, there is a positive association between the independent and dependent variables, except for board size. Following is a detailed discussion of the correlation analysis's findings:

The coefficient of correlation between Board Size (BZ) and Return on Asset (ROA), which is displayed in Table 4.2 below, was -0.231 , indicating negative but statistically significant association at the 0.01 or 1% level of significance. This suggests that large board size is often thought to provide diverse expertise and oversight, however, empirical evidences, particularly in Ethiopian context, shows negative relationship with ROA. This finding is consistent with the agency theory, which suggests that beyond a certain point, increasing board size leads to coordination problems, diluted responsibility and slower decision making. This is further supported by the study of Getachew (2017) and Abate (2019), who observed that small, well-structured boards in Ethiopian banks were more effective in decision-making and improving organizational performance. Table 4.2 below also suggests that there is a strong and positive association between Frequency of Board Meeting and organizational performance. Frequency of board meeting is often associated with better performance because they signal active monitoring and responsiveness to operational and financial issues. This is supported by stewardship theory, which argues that regular engagement enhances oversight and strategic alignment. The finding is also supported by Tadesse (2019) and Anderson et al. (2019), who found that banks with more frequent board meetings

experienced better financial outcomes, due to timely intervention in key decisions. However, too many meetings without agenda could also lead to inefficiency.

Table4.2: Correlation Coefficient Matrix

	Correlations						
	ROA	BZ	FBM	BGD	DEQ	DISE	CEC
ROA	1						
BZ	-.231**	1					
FBM	.292**	-.213**	1				
BGD	.144**	-.183**	.165**	1			
DEQ	.345**	-.152**	.222**	.258**	1		
DISE	.263**	-.195**	.192**	.208**	.334**	1	
CEC	.364**	-.122	.242**	.172**	.283**	.274**	1
**. Correlation is significant at the 0.01 level (2-tailed).							
ROA = Return On Asset, BZ = Board Size, FBM = Frequency of Board Meeting, BGD = Board Gender Diversity, DEQ = Directors' Educational Qualifications, DISE = Directors' Industry Specific Experience, CEC = Chief Executive's Compensation							

Source: Results of Own Survey Data (2025)

Another variable employed in the study was Board Gender Diversity. The coefficient of correlation between Board Gender Diversity (BGD) and Return on Asset (ROA) is 0.144, which specifies that there is a very strong and positive association between Board Gender Diversity and Bank Performance and the relationship is significant at 0.01 or 1% level of significance as shown in Table 4.2 above. This implies that gender-driven boards are thought to improve financial performance by fostering different perspectives, reducing group thinking, and enhancing ethical decision making. This aligns with resource dependence theory, which views diversity as a valuable resource. This finding is also in line with the

finding of Tesfaye (2018), who implied a positive, though sometimes statistically insignificant, relationship between gender diversity and ROA, indicating the potential but underutilized benefit of inclusive boards.

According to Table 4.2 above, the correlation between Directors' Educational Qualification (DEQ) and Return on Asset (ROA) was 0.345. According to this graph, there is a substantial (1% level of significance) association between Return on Asset (ROA) of the selected commercial banks and the Directors' Educational Qualification. This suggests that highly educated board members can better understand complex financial statements, risk management and regulatory requirements. This in turn supports better decision making, aligning with human capital theory, which posits that knowledge and skills improve performance outcomes. This finding is also consistent with the finding of Melaku (2016), who found a positive correlation between Directors' Educational Qualification and ROA in Ethiopian Banks, though significance varied.

The study also used Directors' Industry Specific Experience (DISE) as a variable. According to Table 4.2 above, there is a strong and positive correlation between Directors' Industry Specific Experience and Bank Performance, and the relationship is significant at the 1% level of significance. The coefficient of correlation between Directors' Industry Specific Experience (DISE) and Return on Asset (ROA) is 0.263. This means that industry specific experience allows board members to make more informed strategic decisions, understand industry dynamics and mitigate risks. This is also linked to upper echelons theory, which suggests executives' backgrounds shape firm outcomes. This finding is in line with the finding of Kebede (2017), who reported that directors with financial sector experience improved performance of the bank through making critical timely and informed decisions.

Still according to Table 4.2 above, the correlation between Chief Executives' Compensation (CEC) and Return on Asset (ROA) was 0.364. According to this graph, there is a substantial (1% level of significance) association between Return on Asset (ROA) of the selected commercial banks and the Chief Executives' Compensation (CEC). According to agency theory, aligning CEO compensation with performance motivates executives to act in shareholders' interests. Well-structured compensation plans can enhance accountability and financial performance of the firms. This finding aligns with the finding of Ayele (2020), who

found a positive and statistically significant relationship between CEO compensation and ROA among Ethiopian banks, indicating that performance-based incentives can derive better outcomes.

4.2.2. Multiple Linear Regression Analysis

In this study, multiple linear regression analysis was used to assess the predictive power of the variables under investigation in order to ascertain the influence of the relationship between the independent variables of Corporate governance dimensions (i.e., Board Size, Frequency of Board Meeting, Board Gender Diversity, Directors' Educational Qualification, Directors' Industry Specific Experience and Chief Executives' Compensation) on the dependent variable, which is Bank performance (Measured in ROA). SPSS version 23 was used to code, enter, and compute the multiple regression measurements. Through the use of independent and dependent variables, multiple regression analysis can explain or forecast variance in a dependent variable. The degree of this effect on the dependent variable is determined by the coefficient of determination, also known as R square (Hair et al., 2010). The higher the coefficient, the stronger the effect of the independent variable on the dependent variable. Using the coefficients or beta weights for each independent variable, the researcher can compare the relative significance of each independent variable. This study presents the unstandardized and standardized coefficients for various regression equations. However, remarks are based on unstandardized coefficients for each variable.

4.2.2.1. Tests of Multiple Regressions Assumptions

This section presents the test for the assumptions of classical linear regression model (CLRM) namely the error have zero mean, hetroskedastiy, autocorrelation, normality and multicollinearity. Therefore, before applying the regression model, the aforementioned presumptions were verified:

Detecting Outliers

Given that it uses statistics, multiple regressions are particularly susceptible to outliers (very high or low scores). When screening the raw data, the researcher used Skewness and Kurtosis to look for extreme results. The six structures' Kurtosis and Skewness exhibited normal behavior. The values of Skewness and Kurtosis in Table 4.1 below are between -1 and +1,

indicating that there were no outliers or risky values that would have jeopardized the validity of the analysis.

Table4.3: The Study Variables Skewness and Kurtosis Values

Study Variables	Skewness	Kurtosis
Board Size	-0.110	-0.979
Frequency of Board Meeting	-0.136	-0.647
Board Gender Diversity	-0.116	-0.785
Directors' Educational Qualifications	-0.319	-0.130
Directors' Industry Specific Experience	- 0.060	-0.579
Chief Executives' Compensation	-0.121	-0.622
Return on Asset	0.062	-0.729

Source: Results of Own Survey Data (2025)

Homoscedasticity (variance of the errors is constant ($\text{Var}(ut) = \alpha^2 <$)

Table4.4 Heteroskedasticity Test: White

F-statistic	2.022109	Prob. F(44,45)	0.0103
Obs*R-squared	59.76998	Prob. Chi-Square(44)	0.0567
Scaled explained SS	31.30733	Prob. Chi-Square(44)	0.9247

Source: Survey Data (2025)

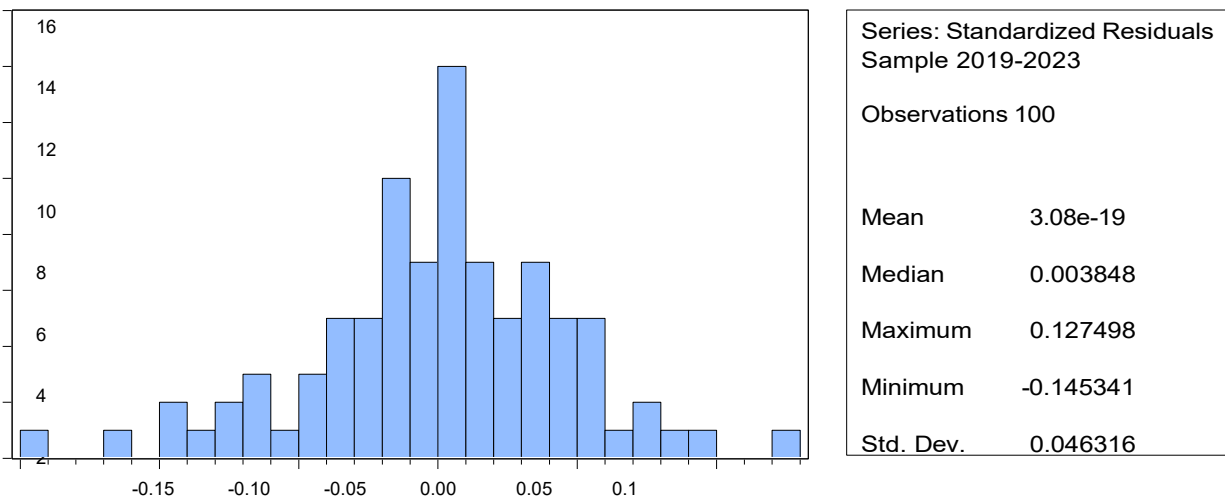
In the table 4.4 shown above the F-statistic shows as there is presence of heteroscedasticity since the p-values were less than 0.05 but Chi-Square versions of the test statistic and the

third version of the test statistic, Scaled explained SS, which as the name suggests is based on a normalized version of the explained sum of squares from the auxiliary regression, gave that there is no evidence for the presence of heteroscedasticity problem. Since both the p value was in excess of 0.05. Therefore, the conclusion of the test is somewhat ambiguous in this case. But as noted by Wooldridge (2002) existence of heteroskedasticity would not cause the parameter estimates to be biased and even in the presence of heteroscedasticity, more efficient estimation is possible provided that other assumptions are met.

The Normality Test

Since the mean value was about close to zero (0) or (mean = $-1.84E-15$) and the standard deviation value was roughly close to one (1) or (Std. Dev. = 0.990), the histogram in Figure 4.1 below suggested that the data were acceptable for normalcy.

Figure4.1: Histogram of the Regression Model

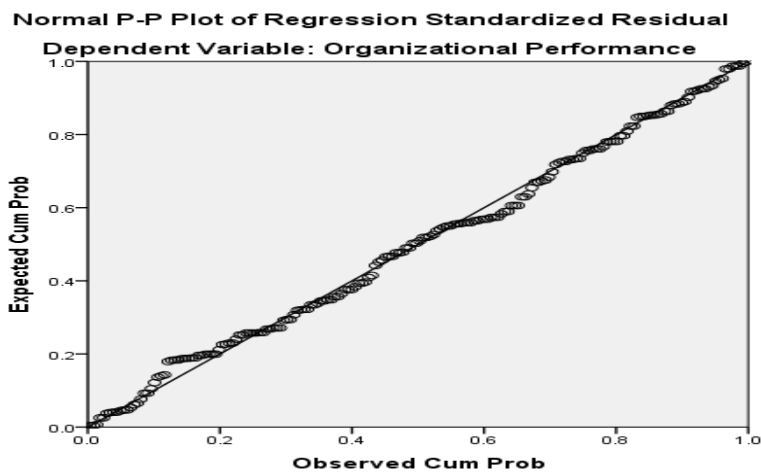


Source: Survey Data (2025)

Tests for Linearity

The little circles in the normal Predicted Probability (P-P) plot in Figure 4.2 showed that they were close to or followed the normality or the diagonal line, indicating the linearity of the data. Linearity is defined as the relationship between the predictor variables and the outcome variable in the regression having a straight line, or when the little circles in the P-P plot are close to the diagonal line.

Figure 4.2: The Normal P-P Plot of the Regression Model



Source: Results of Own Survey Data (2025)

A Multicollinearity Test

Multicollinearity happens when the research predictor variables are strongly correlated with one another. Association coefficients must be less than 0.90 to qualify as multicollinear, while tolerance and Variance Inflation Factor (VIF) values must be greater than 0.1 and less than 10 to qualify as multicollinear, respectively (Hair et al., 2010). According to Tables 4.4

above, the correlation coefficients for each predictor variable were less than 0.90. Additionally, as shown in Tables 4.5 below, all of the model's results had a tolerance value greater than 0.1 and a VIF lower than 10, indicating that the survey data did not exhibit any discernible multicollinearity and that the study's predictor variables did not exhibit strong correlations with one another.

Table 4.5: Multicollinearity Test

Variables	Tolerance	VIF
Board Size	0.347	2.879
Frequency of Board Meeting	0.220	4.550
Board Gender Diversity	0.289	3.463
Directors' Educational Qualifications	0.385	2.600
Directors' Industry Specific Experience	0.353	2.237
Chief Executive's Compensation	0.297	3.231

Source: Results of Own Survey Data (2025)

Six predictors of multiple linear regression models were put forth in an effort to determine the most effective collection of predictors of Organizational Performance, measured in terms of Return on Asset. Board Size (X_1), Frequency of Board Meeting (X_2), Board Gender Diversity (X_3), Directors' Educational Qualifications (X_4), Directors' Industry Specific Experience (X_5), and Chief Executive's Compensation (X_6) were the six predictor variables. The proposed multiple linear regression models' equation was as follows:

$$ROA_{it} = \beta_0 + \beta_1 BZ_{it} + \beta_2 FBM_{it} + \beta_3 BGD + \beta_4 DEQ + \beta_5 DISE + \beta_6 CEC + \varepsilon_{it}$$

Where: β_0 = Constant, ε = Error

As shown in the regression model summary of Table 4.6 below, the R-squared and Adjusted R-squared statistic of the model were 0.899 or (89.9%) and 0.897 or (89.7%) respectively. The explanatory power of the independent variables such as Board Size, Frequency of Board

Meeting, Board Gender Diversity, Directors’ Educational Qualifications, Directors’ Industry Specific Experience, and Chief Executive’s Compensation on the changes in dependent variable (bank performance) was 89.9%. The result of Adjusted R-squared shows that changes on Return on Asset (ROA) was explained 89.7% by the independent variables employed in this study. As a result, other factors beyond the scope of this model or study were responsible for the remaining 10.3% of the changes in the dependent variable (ROA).

Given the structure of the data—panel data consisting of five commercial banks observed over a five-year period (2019–2023)—this study employed a panel data regression model to examine the effect of corporate governance mechanisms on financial performance (as measured by Return on Assets). Panel data models are preferred in this context because they control for unobserved heterogeneity across banks and improve estimation efficiency by using both cross-sectional and time-series variations.

To determine the most appropriate model between Fixed Effects (FE) and Random Effects (RE), a Hausman test was conducted. The test results indicated that the Fixed Effects model was more appropriate, suggesting that unobserved individual-specific effects are correlated with the independent variables. Consequently, the Fixed Effects model was used for regression analysis to ensure unbiased and consistent estimators of the relationships between governance variables (board size, meeting frequency, gender diversity, education, industry experience, and CEO compensation) and financial performance. This model allows the study to isolate the effects of time-invariant characteristics of each bank, providing more robust insight into the effect of internal corporate governance mechanisms on financial performance.

Table 4.6: Model Summary of the Regression Analysis

Model Summary^b				
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.948 ^a	.899	.897	1.47765
a. Predictors: (Constant), Board Size, Frequency of Board Meeting, Board Gender Diversity, Directors’ Educational Qualifications, Directors’ Industry Specific Experience,				

and Chief Executive's Compensation
b. Dependent Variable: Return on Asset

Source: Results of Own Survey Data (2025)

The ANOVA result in Table 4.7 below shows the F-statistics and probability (F-statistics) for the regression. At a 1% level of significance, the F-statistic's null hypothesis which states that the Adjusted R-squared is equal to zero was rejected. F-value of 0.000 shows strong statistical significance which enhanced the reliability and validity of the model. This shows that the calculated linear regression model line's slope is greater than zero, demonstrating that there is a linear relationship between all four predictor variables (i.e., Board Size, Frequency of Board Meeting, Board Gender Diversity, Directors' Educational Qualifications, Directors' Industry Specific Experience, and Chief Executive's Compensation) and Organizational Performance or Return on Asset. This indicates that the six predictor variables significantly predict Return on Asset (ROA).

Table 4.7: Results of the Analysis of Variance (ANOVA)

ANOVA ^a						
Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	3672.586	4	918.146	420.503	.000 ^b
	Residual	412.672	189	2.183		
	Total	4085.258	193			
a. Dependent Variable: Return on Asset (ROA)						
b. Predictors: (Constant), BZ, FBM, BGD, DEQ, DISE, CEC						

Source: Results of Own Survey Data (2025)

Based on the commonly used multiple regression method (Table 4.8 below), it was determined that all six independent or predictor factors were significant in explaining

organizational performance. Or the variation in the dependent variable Return on Asset (ROA) was strongly influenced by all the independent variables.

Table4.8: Analysis of the Regression Model Coefficients

Coefficients ^a						
Model		Unstandardized Coefficients		Standardized Coefficients	T	Sig.
		B	Std. Error	Beta		
1	(Constant)	-2.303	.878		-4.900	.000
	BZ	-0.172	.050	.135	3.518	.001
	FBM	.201	.021	.473	3.458	.000
	BGD	.121	.044	.151	4.716	.001
	DEQ	.211	.068	.279	5.536	.000
	DISE	.193	.044	.151	5.488	.001
	CEC	.213	.068	.279	7.481	.000
a. Dependent Variable: Return on Asset (ROA)						
BZ = Board Size, FBM = Frequency of Board Meeting, BGD = Board Gender Diversity, DEQ = Directors' Educational Qualifications, DISE = Directors' Industry Specific Experience, and CEC = Chief Executive's Compensation						

Source: Results of Own Survey Data (2025)

The regression coefficients in Table 4.8 above were considered significant at the 95% level, yielding an alpha value of 5%. As a consequence, the unstandardized beta coefficients for Board Size, Frequency of Board Meeting, Board Gender Diversity, Directors' Educational Qualifications, Directors' Industry Specific Experience, and Chief Executive's Compensation were -0.172, 0.201, 0.121, 0.211, 0.193, and 0.213 accordingly from the regression result.

According to Table 4.18 above, the predicted model looked like this:

$$Y(\text{ROA}) = -2.303 - 0.172X_1 + 0.201X_2 + 0.121X_3 + 0.211X_4 + 0.193X_5 + 0.213 X_6$$

The unstandardized beta coefficients of the regression model in Table 4.8 above indicated that Chief Executives' Compensation have the largest positive and significant effect on Return on Asset ($\beta_6 = 0.213$, $t = 7.481$, $p < 0.05$). This means that one unit increase in CEO

compensation leads to 0.213 increase in ROA. This is the strongest positive coefficient suggesting that well compensated CEOs are likely motivated to align their interests with shareholders. From an agency theory perspective, performance linked compensation mitigates principal-agent problems. This finding is consistent with the finding of Getachew (2020), who stated similar trends in Ethiopian banks, where higher paid CEOs, especially with performance bonuses, demonstrated better asset utilization and profitability outcomes. Secondly, followed by the unstandardized beta coefficients of Directors' Educational Qualifications with ($\beta_4 = 0.211$, $t = 5.536$, $p < 0.05$), which suggested that Directors' Educational Qualifications has a positive and significant effect on ROA. This suggests that a unit rise in Directors' Educational Qualifications will result a 0.211 growth in ROA. This positive effect aligns with the findings by Mahlet (2021), indicating that highly educated directors bring analytical skills, strategic vision, and better understanding of complex financial products and risks. From accounting and finance perspective, such boards are more capable of interpreting financial statements, understanding audit issues and making risk-informed decisions. In the third place was Frequency of Board Meeting with ($\beta_2 = 0.201$, $t = 3.458$, $p < 0.05$) was the third highest positive and significant value to have an effect on Bank Performance. This implies that a unit increase in board meetings is associated with 0.201 increases in ROA. This positive relationship supports the argument from stewardship theory, suggesting that frequent meetings enhance monitoring, strategic discussion and compliance. Empirical evidence from Mahlet (2021) confirms that Ethiopian commercial banks with more frequent board meeting respond faster to regulatory and operational issues, improving performance. In the fourth place was Directors' Industry Specific Experience with ($\beta_5 = 0.193$, $t = 5.488$, $p < 0.05$) was the fourth highest positive and significant value to have an effect on Bank Performance. This implies that a unit increase in relevant industry specific experience leads to a 0.193 increase in ROA. This positive relationship is consistent with human capital theory, which states that directors with banking-specific knowledge improve strategic oversight, risk management and regulatory compliance. Yenesew (2019) notes that Ethiopian banks with experienced board members adopt better to NBE policy changes and innovate within tight regulatory framework. In the fifth in place was Board Gender Diversity with ($\beta_3 = 0.121$, $t = 4.716$, $p < 0.05$) was the fourth highest positive and significant value to have an effect on Bank Performance. The beta value implies that unit increase in gender

diversity leads to a 0.121 increase in ROA and this finding is consistent with the resource-based view, where diverse boards bring varied perspectives, innovative ideas and enhanced governance oversight. In male dominated board environments like Ethiopian corporate environment, even modest increase in female representation may significantly effect performance (Yenesew, 2019). This finding also aligns with global studies showing gender diverse boards reduce group thinking and enhance reputation. Finally, Board Size had scored the negative and significant value to have an effect on Return on Asset with ($\beta_1 = -0.172$, $t = 3.518$, $p < 0.05$). This indicated that one unit rise in Board Size beyond the optimum is followed by a 0.172 unit decrease in Return on Asset, holding other factors constant. This negative relationship aligns with the agency theory and resource dependency theory, which states that larger boards may suffer from coordination issues, communication inefficiencies and diluted accountability. In Ethiopian banking context, Mahlet (2021) and Amasu (2017), excessively large boards are slow in responding to market changes and often function less effectively. Optimal board size allows for better monitoring without bureaucratic overload.

4.3. In-Depth Interview Results

The interviews were conducted with the board chairmen of the selected five commercial banks namely, CBE, AB, BOA, DB and COOP. A total of four peoples were interviewed at different times. In this study, the interview was totally unstructured. All the interviewees have got an education level of at least a first degree in a business related area and have ample working experience in the banking industry. Hence, they were believed to have a good knowledge and experience in corporate governance. The interviews were conducted independently with each director.

The interviewees rise board of director's motivation or directors desire to attend meetings, read materials, spend time on corporate activities, and to make decisions that contribute to organizational success. Motivated directors desire to information about the operations and management of the organization as well as information about the business environment, the performance and activities of competitors which is vital factors lead board of directors effectiveness that enhance performance of companies. Further they noted there is lack of motivation and commitment of directors which hamper company performance and the challenging part of working in groups.

The interviewees also pointed out as corporate transparency and disclosure is weak in case of Ethiopia. Effective legal framework that identifies the specific disclosure requirements didn't exist in the country. Furthermore, they noted that in Ethiopia issues on corporate governance disclosure such as; financial disclosures, non-financial disclosures, annual general meetings timing and means of disclosure and best practices for compliance with corporate disclosure are very low.

The interviewees also rise about board member ability to translate broad knowledge into good strategic decisions and they suggest board members' human capital in terms of background and experience certainly influences the outcomes of board decision-making. This knowledge involves technical expertise concerning areas needed to govern effectively, such as business strategy, succession, finance, law, government, technology, society and how organizations operate as general this lead qualified decision that lead financial performance. But the problem is with director's experience and qualification as there are few directors that have prior experience in banking sector and qualified directors in the board.

Another issue mentioned by the interviewees was there is no appropriate national code of corporate governance adopted in the country except the commercial code which needs major improvements as per the interview conducted with Ethiopia commercial banks board chairman. Regarding banks' board size there is no problem with board size of the banks. Boards of directors are expected to prove strategic leadership to the company by include supervision of corporate governance along with the monitoring of strategic area including internal control and risk management. The board is also expected to reviews the management of corporate resources (human resource finance and information) thus effective and efficient leadership of the board can be realized through full board members and board committees that monitors thematic area such organization demand.

As per discussion the size of the board should be adequate. As the participant point out board size have no problem. This is also evidenced that the regulatory requirement under Article 347 of the Commercial Code of Ethiopia (1960), states that a share company should have a board size of between 3 and 12 members only accordingly all commercial banks have a board size of seven to twelve.

The interviewees point out as professionals with requisite technical skill and experience should head and manage commercial banks. This practice promotes professionalism in the industry. The need for strong internal control system was emphasized, in order to promote good corporate governance and improve the image of the Ethiopia banking industry.

The interviewees also suggest that the proposed corporate governance guideline for the financial sectors as general and specifically for the banking industry can enhance commercial banks' growth in Ethiopia. Putting governance guidelines promotes health of the industry and keeps interest of all stakeholders in sectors and avoids sectors systemic collapse. But when we add this guideline to our list of directives (law) we should take a great care in analyze pros and con of each issue included in guideline.

They underline their arguments by indicating as nature of governance practices are not endogenous one country governance nature may not exact fit to other country governance practice. So when we adopt/develop its batter if it can be supported by in-depth research and further they note as the proposed corporate governance guideline need sort of correction.

4.4.Hypothesis Test Results

The Pearson correlation model and multiple linear regression models tested the six hypotheses of this research paper concerning The effects of Corporate Governance on the Financial Performance of Commercial Banks of Ethiopia, according to the regression tables above, the p-value was used to determine if the hypothesis is true or false and was based on the beta and correlation coefficient with a 95 percent confidence level.

Hypothesis - 1

H1: Board size has a positive and significant effect on Bank Performance.

The unstandardized beta coefficient with ($\beta_1 = -0.172$, $t = 3.518$, $p < 0.05$) indicated that bank Board Size had a negative and significant effect on financial performance of the commercial bank. The regression analysis as presented in Table 4.8 above supports this finding. This indicated that one unit rise in Board Size beyond the optimum is followed by a 0.172 unit decrease in Return on Asset, holding other factors constant. This negative relationship aligns with the agency theory and resource dependency theory, which states that larger boards may

suffer from coordination issues, communication inefficiencies and diluted accountability. In Ethiopian banking context, Mahlet (2021) and Amasu (2017), excessively large boards are slow in responding to market changes and often function less effectively. Optimal board size allows for better monitoring without bureaucratic overload. Therefore the hypothesis stating Board size has a positive and significant effect on Bank Performance has been rejected.

Hypothesis - 2

H2: Board frequency of meeting has a positive and significant effect on Bank Performance.

The unstandardized beta coefficient with ($\beta_2 = 0.201$, $t = 3.458$, $p < 0.05$) indicated that Board Frequency of Meeting has a positive and significant effect on Bank Performance, and the regression analysis as presented in Table 4.8 above supports this finding. This implies that a unit increase in board meetings is associated with 0.201 increases in ROA. This positive relationship supports the argument from stewardship theory, suggesting that frequent meetings enhance monitoring, strategic discussion and compliance. Empirical evidence from Mahlet (2021) confirms that Ethiopian commercial banks with more frequent board meeting respond faster to regulatory and operational issues, improving performance.

Hypothesis - 3

H3: Board gender diversity has a positive and significant effect on Bank Performance.

The unstandardized beta coefficient with ($\beta_3 = 0.121$, $t = 4.716$, $p < 0.05$) indicated that Board gender diversity has a positive and significant effect on Bank Performance. The regression analysis as presented in Table 4.8 above supports this finding. This finding is consistent with the resource-based view, where diverse boards bring varied perspectives, innovative ideas and enhanced governance oversight. In male dominated board environments like Ethiopian corporate environment, even modest increase in female representation may significantly effect performance (Yenesew, 2019). This finding also aligns with global studies showing gender diverse boards reduce group thinking and enhance reputation.

Hypothesis - 4

H4: Directors' educational qualification has a positive and significant effect on Bank Performance.

The unstandardized beta coefficient with ($\beta_4 = 0.211$, $t = 5.536$, $p < 0.05$) indicated that Directors' educational qualification has a positive and significant effect on Bank Performance. The regression analysis as presented in Table 4.8 above supports this finding.

This suggests that a unit rise in Directors' Educational Qualifications will result a 0.211 growth in ROA. This positive effect aligns with the findings by Mahlet (2021), indicating that highly educated directors bring analytical skills, strategic vision, and better understanding of complex financial products and risks. From accounting and finance perspective, such boards are more capable of interpreting financial statements, understanding audit issues and making risk-informed decisions.

Hypothesis - 5

H5: Directors Industry Specific experience has a positive and significant effect on Bank Performance.

The unstandardized beta coefficient with ($\beta_5 = 0.193$, $t = 5.488$, $p < 0.05$) indicated that Directors Industry Specific experience has a positive and substantial effect on Bank Performance, and the regression analysis as given in Table 4.88 above supports this finding. This implies that a unit increase in relevant industry specific experience leads to a 0.193 increase in ROA. This positive relationship is consistent with human capital theory, which states that directors with banking-specific knowledge improve strategic oversight, risk management and regulatory compliance. Yenesew (2019) notes that Ethiopian banks with experienced board members adopt better to NBE policy changes and innovate within tight regulatory framework.

Hypothesis - 6

H6: Chief executive Compensation has a positive and significant effect on Bank Performance.

The unstandardized beta coefficient with ($\beta_2 = 0.213$, $t = 7.481$, $p < 0.05$) indicated that Chief executive Compensation has a positive and significant effect on Bank Performance, and the regression analysis as presented in Table 4.8 above supports this finding. This means that one unit increase in CEO compensation leads to 0.213 increase in ROA. This is the strongest positive coefficient suggesting that well compensated CEOs are likely motivated to align their interests with shareholders. From an agency theory perspective, performance linked compensation mitigates principal-agent problems. This finding is consistent with the finding of Getachew (2020), who stated similar trends in Ethiopian banks, where higher paid CEOs,

especially with performance bonuses, demonstrated better asset utilization and profitability outcomes.

Table4.9: Summary of Hypothesis Testing

Hypothesis	P-value	Expected Effect	Result	Decision Accepted/Rejected
H1: Board size has a positive and significant effect on Bank Performance.	0.001	Positive	Negative	Rejected
H2: Board frequency of meeting has a positive and significant effect on Bank Performance.	0.000	Positive	Positive	Accepted
H3: Board gender diversity has a positive and significant effect on Bank Performance.	0.001	Positive	Positive	Accepted
H4: Directors' educational qualification has a positive and significant effect on Bank	0.000	Positive	Positive	Accepted

Performance.				
H5: Directors Industry Specific experience has a positive and significant effect on Bank Performance.	0.001	Positive	Positive	Accepted
H6: Chief executive Compensation has a positive and significant effect on Bank Performance.	0.000	Positive	Positive	Accepted

Source: Results of Own Survey Data (2025)

CHAPTER FIVE

CONCLUSIONS AND RECOMMENDATIONS

This chapter contains of the deductions drawn from the analysis part and the suggestions forwarded by the investigator so as to advance the effects of corporate governance on financial performance of commercial banks in Ethiopia.

5.1. Conclusions

This study examined the effects of selected corporate governance variables on the financial performance of commercial banks in Ethiopia, using Return on Assets (ROA) as the dependent variable. The analysis was conducted using panel data from 5 commercial banks over a 5-year period (2019–2023) and each year having 4 quarters (5 banks * 5Years*4 quarters) , yielding 100 observations. The governance indicators considered include Board

Size (BZ), Frequency of Board Meetings (FBM), Board Gender Diversity (BGD), Directors' Educational Qualifications (DEQ), Directors' Industry-Specific Experience (DISE), and Chief Executive Officer Compensation (CEC).

The regression results revealed that five of the six explanatory variables—FBM, BGD, DEQ, DISE, and CEC—had positive and statistically significant relationships with ROA, indicating that improvements in these governance mechanisms are associated with better financial performance of banks. Conversely, Board Size (BZ) exhibited a negative and significant relationship with ROA, suggesting that larger boards may be detrimental to financial performance, possibly due to communication inefficiencies and slower decision-making.

The positive coefficient of Frequency of Board Meetings (0.201) suggests that regular and proactive board engagement is crucial for effective oversight, monitoring, and responsiveness to financial and operational issues. The significance of Board Gender Diversity (0.121) confirms that inclusive governance contributes to diverse perspectives, better risk management, and stakeholder trust supporting global literature advocating for greater female representation in boardrooms. The finding that Directors' Educational Qualification (0.211) and Industry-Specific Experience (0.193) positively affect performance underscores the value of competent and experienced leadership. Highly educated and sector-experienced board members are likely to be better informed, more strategic, and capable of steering complex institutions in a competitive environment. Finally, the strong positive association between CEO Compensation and ROA (0.213) highlights the importance of incentive-aligned remuneration. This supports agency theory, which posits that performance-based compensation can mitigate managerial self-interest and foster accountability toward shareholders' wealth maximization. In contrast, the negative relationship between Board Size and ROA (-0.172) aligns with theoretical and empirical findings suggesting that overly large boards may suffer from diminished efficiency and accountability. This result underscores the need for Ethiopian commercial banks to adopt optimal board structures that balance diversity and functionality.

The findings collectively emphasize that corporate governance is not merely a compliance mechanism but a strategic tool for enhancing financial performance. Sound governance

practices particularly those promoting competence, engagement, diversity, and well-designed incentives are instrumental in ensuring bank profitability and sustainability.

5.2. Recommendations

This study was aimed to investigate the effects of selected corporate governance variables on the financial performance of commercial banks in Ethiopia. The researcher provided the following recommendations, which may have managerial, corporate governance and performance implications, based on the data and conclusions reached:

- Optimize Board Size for Effective Oversight

Since the study found a negative relationship between board size and ROA, commercial banks are advised to maintain an optimal board size—neither too small to lack diversity nor too large to impede decision-making efficiency. The National Bank of Ethiopia (NBE), as the regulatory body, should provide clearer guidelines on the ideal board size to promote effective corporate governance practices across the banking sector.

- Increase the Frequency and Effectiveness of Board Meetings

The significant positive effect of board meeting frequency on ROA suggests that more frequent and focused meetings contribute to better monitoring and strategic direction. Banks should ensure that board meetings are held regularly with well-structured agendas that address performance, compliance, and risk issues. The quality of discussions and timely follow-up on resolutions must be prioritized, not just the quantity of meetings.

- Promote Gender Diversity on Bank Boards

The positive coefficient for Board Gender Diversity (BGD) indicates that gender-inclusive boards enhance performance. Therefore, banks should actively promote gender diversity by implementing affirmative recruitment policies, leadership development programs for women, and a culture that values diversity. The NBE and other stakeholders may consider setting minimum gender inclusion thresholds to encourage this shift.

- Strengthen the Recruitment of Highly Educated and Experienced Board Members

Since educational qualification (DEQ) and industry-specific experience (DISE) positively influence ROA, it is recommended that commercial banks adopt competency-based criteria for selecting board members. Regulators should enforce policies that ensure board members possess advanced qualifications in finance, accounting, economics, or law and have practical experience in banking or related sectors.

- Align CEO Compensation with Performance Metrics

The strong positive relationship between CEO compensation (CEC) and ROA underscores the importance of performance-based incentives. Banks should design transparent, merit-based compensation frameworks that link executive pay to key performance indicators such as profitability, asset quality, and risk management. This would align managerial incentives with shareholder interests and encourage long-term value creation.

- Strengthen Governance Guidelines and Regulatory Oversight

The National Bank of Ethiopia should review and strengthen corporate governance guidelines to reflect the findings of this and similar studies. Emphasis should be placed on board functionality, composition, and accountability, as well as periodic evaluation of governance practices to ensure alignment with global standards and local realities.

- Encourage Capacity Building and Training

To enhance governance effectiveness, regular training and development programs should be provided for board members and senior executives on topics such as risk management, corporate ethics, financial oversight, and regulatory compliance. Such capacity-building initiatives can improve decision-making quality and overall bank performance.

5.3. Implications for Future Research

This study was conducted to investigate the effects of corporate governance on financial performance of commercial banks in Ethiopia. The sample was drawn only from the selected commercial banks in Ethiopia, thus this study may be limited in its generalizability of all banks operating in the country. So, future researchers should have to draw sample of

respondents from other banks and branches operating in the country for the sake generalizing the results of the study.

Future research could be extended to include microfinance institutions, commercial banks companies, and investment firms, to examine whether the effects of corporate governance vary across different financial sectors. This broader scope would enrich the generalizability of the findings and inform sector-specific policy recommendations. This study focused on six corporate governance variables.

Future studies may incorporate other relevant factors such as: Audit committee independence, Ownership structure, Board independence, CEO duality These variables could provide a more comprehensive understanding of how governance mechanisms influence financial performance.

This study employed Return on Assets (ROA) as the sole measure of financial performance. Future researchers may consider using Return on Equity (ROE), Net Interest Margin (NIM), or Earnings Per Share (EPS) to examine whether the results are consistent across different financial performance indicators. This study was primarily quantitative. Future research could adopt a mixed-methods approach, combining statistical analysis with qualitative interviews or case studies. This would offer deeper insight into the practical dynamics of governance practices, decision-making culture, and regulatory challenges.

Future research may consider conducting comparative studies between private and state-owned banks, or between Ethiopian and other Sub-Saharan African banks, to examine how institutional, legal, and cultural differences shape governance-performance relationships. A longitudinal study over a longer time horizon could also reveal long-term trends and the evolving role of governance in financial performance.

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APPENDICES

Appendix 1: Interview Questions

Addis Ababa University

College of Business and Economics

Department of Accounting and Finance

Title: Effects of Corporate Governance on Financial Performance of Commercial Banks in Ethiopia

Target Respondents: Board Members and Senior Executives of Commercial Banks in Ethiopia

Data Collection Method: Semi-structured Interview (face-to-face or virtual)

SECTION A: INTRODUCTORY QUESTIONS

1. Can you briefly describe your role and how long you have served on the board or executive team of this bank?
2. What is your academic and professional background, especially as it relates to banking or finance?
3. Can you briefly comment on how you define financial performance in your board discussions?

SECTION B: CORPORATE GOVERNANCE VARIABLES

I. Board Size

4. How many members currently serve on the board of directors of your bank?
5. Do you think the current size of the board enhances or hinders effective governance and decision-making? Please explain.

II. Board Meeting Frequency

6. How often does the board meet (monthly, quarterly, etc.)?
7. In your opinion, how does the frequency of meetings affect the board's ability to monitor management and make timely decisions?
8. Are special or emergency board meetings held when necessary? Please provide examples.

III. Board Gender Diversity

4. How many women currently serve on your board?
5. In your view, what influence does gender diversity have on board discussions, decisions, and overall performance?
6. Have you observed any changes in performance or culture due to increased gender diversity?

IV. Directors' Educational Qualification

7. What are the typical educational qualifications of board members in your bank?

8. To what extent do you believe that educational background contributes to board effectiveness and sound financial decision-making?
9. Do you consider advanced degrees (e.g., MBA, PhD) to be essential for better governance? Why or why not?

V. Directors' Industry-Related Experience

10. How many board members have prior experience in banking or financial services?
11. Do you believe that having industry experience among directors leads to better financial oversight or performance outcomes? Please elaborate.
12. Can you share examples of how industry experience has contributed to major strategic or financial decisions?

VI. CEO Compensation

13. How is the CEO's compensation package structured (e.g., fixed salary, performance-based bonuses, stock options)?
14. Is there a clear link between CEO compensation and the bank's financial performance indicators like ROA?
15. What challenges have you encountered in aligning CEO incentives with long-term bank performance?

SECTION C: FINANCIAL PERFORMANCE (ROA)

16. To what extent does the board monitor and evaluate financial performance using metrics such as Return on Assets (ROA)?
17. Do board decisions explicitly consider how they will effect ROA or other performance indicators?
18. Have you observed a correlation between corporate governance practices and improvements (or declines) in ROA in recent years?

SECTION D: WRAP-UP AND REFLECTION

19. In your opinion, what are the most critical aspects of corporate governance that positively influence financial performance?
20. What challenges do you face in improving corporate governance in your bank?

21. Is there anything else you'd like to add that you believe is relevant to this research?

Appendix Two: Row Data

COMMERCIAL BANK OF ETHIOPIA (EBE)							
YEAR	ROA	BZ	FBM	BGD	DEQ	DISE	CEC
2019	13%	7	2	1	7	2.00	13.76
2020	11%	7	2	1	7	3.00	11.51
2021	14%	9	2	1	9	3.00	11.61
2022	17%	9	2	1	9	3.00	11.61
2023	19%	7	2	1	7	2.00	11.65

AWASH BANK (AB)

YEAR	ROA	BZ	FBM	BGD	DEQ	DISE	CEC
2019	8%	6	5	0	5	1.00	12.21
2020	4%	5	6	0	4	2.00	12.43
2021	2%	5	6	2	4	2.00	12.43
2022	15%	7	6	1	7	2.00	12.61
2023	16%	6	7	1	6	3.00	12.61

BANK OF ABYSSINIA (BoA)							
YEAR	ROA	BZ	FBM	BGD	DEQ	DISE	CEC
2019	14%	9	39	1	9	5.00	13.53
2020	10%	9	45	1	9	5.00	13.53
2021	10%	9	45	1	9	6.00	13.53
2022	11%	9	40	1	9	6.00	13.59
2023	12%	9	40	1	9	6.00	13.59

DASHEN BANK (DB)							
YEAR	ROA	BZ	FBM	BGD	DEQ	DISE	CEC
2019	6%	5	16	1	6	1.00	12.01
2020	13%	5	16	2	6	2.00	12.04
2021	17%	5	16	2	6	2.00	12.04
2022	12%	5	16	2	6	2.00	12.21
2023	7%	5	16	1	6	2.00	12.24

COOPERATIVE BANK OF OROMIA (COOP)							
YEAR	ROA	BZ	FBM	BGD	DEQ	DISE	CEC
2019	11%	9	21	1	6	5.00	13.53
2020	8%	9	24	0	6	5.00	13.70
2021	8%	9	21	0	6	5.00	13.79
2022	15%	9	21	0	6	5.00	14.01
2023	10%	9	26	0	5	5.00	14.25