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ADDIS ABABA UNIVERSITY  
SCHOOL OF GRADUATE STUDIES  
COLLEGE OF BUSINESS AND ECONOMICS  
DEPARTMENT OF MANAGEMENT

CORPORATE GOVERNANCE PRACTICE AND ITS IMPACTS ON FINANCIAL  
PERFORMANCES: The Case of Zemen Bank Share Company

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This is to certify that the dissertation prepared by Wossenu Abera in this research project entitled “CORPORATE GOVERNANCE PRACTICES AND ITS IMPACTS ON FINANCIAL PERFORMANCES: The Case of Zemen Bank Share Company” and submitted in partial fulfillment of the requirements for the EMBA Degree in Management complies with the regulations of the university and meets the accepted standards with respect to originality and quality.

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### **Declaration**

I hereby declare that the work which is being presented in this research project entitled “CORPORATE GOVERNANCE PRACTICES AND ITS IMPACTS ON FINANCIAL PERFORMANCES: The Case of Zemen Bank Share Company” is my own original work, has not been presented for a degree in any other university; and that all sources of material used for the research project have been duly acknowledged.

**Wossenu Abera**

\_\_\_\_\_

Signature

Date

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## Abstract

*There has been a great deal of attention given to the issue of corporate governance in recent times. To date, the studies made on different aspects of corporate governance largely have focused more on developed economies than emerging economies.*

*Most of the previous research conducted on the Government owned banks including state owned Commercial Bank of Ethiopia and Construction Bank of Ethiopia. The student researcher also noticed inconsistent results of the previous studies about the Corporate Governance practices of banks in Ethiopia.*

*This research assesses the Corporate Governance practices in one of the private banks in Ethiopia, Zemen Bank S.C and assesses the impact of board Corporate Governance variables (board size, board diversity, board sub-committees, Board members educational qualifications and board meetings) on the bank financial performance (ROA).*

*The research applied mixed method approach in the collection and analysis of the data. The qualitative data were collected both from the primary (Questionnaire and Interview) and secondary sources. The findings from the quantitative data analysis based on the regression analysis showed that the board size has positive and significant impact on the financial performance of the bank. The findings also indicated a positive and significant relationship between board diversity and financial performance of the bank. Furthermore, the study revealed that board performance evaluation, corporate governance rating of the bank and Board of directors tailored corporate governance training contribution to improve the Zemen bank financial performance (ROA).*

*This research examines the existing Corporate Governance practices according to the National Bank of Ethiopia and internationally accepted best practices. It forwards recommendations that improve the current practices. Thus, this provides the incentive for other student researcher to contribute and narrow the knowledge gap in this area. This study, therefore, contributes its share to the literature in general for Corporate Governance practices and specifically for the development of the private banking sector in Ethiopia.*

**Key Terms:** Corporate Governance; Board Size, Board Diversity; Bank Performance; Board Evaluation, Corporate Governance Rating, Governance Best Practices.

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## **List of Acronyms**

AGM	Annual General Meeting
ACGN	Africa's Corporate Governance Network
BOD	Board of Directors
CEO	Chief Executive Officer
CG	Corporate Governance
CGR	Corporate Governance Rating
ECA	Economic Commission for Africa
NBE	National Bank of Ethiopia
OECD	Organization for Economic Co-operation and Development
ROA	Return on Asset
SPSS	Statistical Package for Social Sciences
VIF	Variance Inflation Factor

## CHAPTER ONE

### INTRODUCTION

#### 1.1. Background of the Study

The term “Corporate Governance” has a clear origin from a Greek word “Kyberman”, meaning to steer, lead or govern. From the Greek usage of the word, it was adopted into the Latin language where it was referred to as “Gubernare” and the French version known as “governor”. It could also mean the process of decision making and a systemic process by which decisions may be implemented. However, corporate governance has much a different meaning to different organizations (Ayandele & Isichei, 2013).

There has been a great deal of attention given to the issue of corporate governance in recent times. The concept of corporate governance has been a priority on the policy agenda in developed market economies especially among very large firms. Further to that, the concept is gradually warming itself as a priority in the African continent. Indeed, it is believed that the Asian crisis and the relatively poor performance of the corporate sector in Africa have made the issue of corporate governance a catchphrase in the development debate (Berglof & von Thadden, 1999).

A number of recent studies show that good corporate governance is becoming a company top priority. For example, a study by Gompers et al (2003) showed that companies with strong shareholder rights yielded annual returns that were 8.5 percent greater than those with weak rights. Related to that, it was also observed that the more democratic firms also enjoyed higher profits, higher sales growth, and lower capital expenditures.

Again, poorly governed firms are expected to be less profitably, have more bankruptcy risks, lower valuations and pay out less to their shareholders, while well-governed firms are expected to have higher profits, less bankruptcy risks, higher valuations and pay out more cash to their shareholders. Claessens (2003) also argues that better corporate frameworks benefit firms through greater access to financing, lower cost of capital, better performance, and more favourable treatment of all stakeholders. Other researchers contend that good corporate governance is important for increasing investor confidence and market liquidity (Donaldson, 2003).

Banks play a vital role in economic development of our nation. It is important to know how well our financial sector is functioning. Particularly, developing economy like Ethiopia, where there is no capital market, highly depends on the intermediary role of financial institutions for channelling funds to the public. Thus, the banks including the private commercial banks as financial institutions play significant role and contributing a lot in our economy.

Most of the commercial banks in Ethiopia have ended the last fiscal year with positive results although market conditions have changed in the past few years making the outlook for this year and beyond much more challenging. Among all the factors, Corporate Governance is one of the factors that have considerable contribution for the success of the banks. Hence, it becomes important to assess the Corporate Governance practices of banks especially private commercial banks.

Although Corporate Governance is essential to all sectors of the economy, it is however crucial to the banking sector due to the sector's critical role and impact on the entire economy. According to Hambrick et al. (2008), not only do the constituents of banking sector stand to gain or lose due the quality and nature of corporate governance therein, but the entire national systems can be propelled as well. Katrodia (2012) also stated that the health of the economy is closely related to the soundness of its banking sector.

In general, it is important to have a transparent and healthy banking system for the growth and development of the economy. For this reason, this sector needs more supervision and good governance. Sound corporate governance of banks can also lower the investment risk of investors and helps to reduce the cost of financing, which will ultimately introduce a flow of foreign investment into the country.

## **1.2. Rationale of the Study**

The researcher is one of the shareholders of Zemen Bank Share Company. The researcher is personally interested in undertaking research on this specific topic about Zemen Bank Share Company for several reasons. First, the researcher wants to know the real Corporate governance practices of Zemen Bank.

As shareholder of the bank, the researcher knows that the bank has not conducted any Corporate Governance Rating by external rating company or from other professional firm about the status of the bank corporate governance practices. Hence, the researcher wanted to conduct an independent and credible assessment of the bank corporate governance practices. The researcher believes that this information benefits the shareholders and other stakeholders for their future investment decision. It helps shareholders to manage their shareholding in the bank as they can differentiate the status of the bank based on the bank corporate governance practices.

The Second reason is that the focus of this research is on one of the Ethiopian private commercial banks. The importance of this Corporate governance research on the private commercial bank sector could be justified by the following reasons. The first could be related to the limited knowledge about the corporate governance practices in the private bank sectors in Ethiopia. The other reason could also be related to the inconsistent results of the previous studies about the corporate governance practices and its impact on the performance of banks in Ethiopia.

This research assesses the corporate governance practices in one of the private banks in Ethiopia, Zemen Bank S.C and examined the impact of board corporate governance variables (board size, board diversity, board sub-committees, Board members educational qualifications and board meetings) on the bank financial performance(ROA).

The study of the corporate governance practice is very important in emerging economies like Ethiopia because of the differences in the social set up, cultural values and economic conditions compared to developed economies. Bhasa (2004) suggested that countries should develop corporate governance models unique to their needs by understanding their contextual situations. Thus, the empirical findings of studies made in developed economies might have limited application and meaning in emerging economies due to the differences in contextual settings that include organizational and environmental characteristics (Kumar & Zattoni, 2013).

A study of corporate governance is important to Ethiopia mainly because: it is a key to developing a market economy and attracting foreign investment as desiderata for sustainable development; it ensures greater transparency and disclosure and thereby enhances investor

confidence; it also ensures shareholder protection, to mention a few of the many more benefits that accrue (Tsegabirhan, 2015).

Thirdly, the researcher, who worked in the banking sector for several years, is very much interested to know more about the bank industry corporate governance practices. He believes that his research on the bank Corporate Governance practices will be golden and real-life opportunity to know more about it as he has a plan in future to serve in the banking sector as board member.

More importantly as a driving force for this research, much work has not been done on corporate governance in Ethiopia (Kiyota, Peitsch & Stern, 2008). To date, the studies made on different aspects of corporate governance largely have focused more on developed economies than emerging economies (Pamburai, Chamisa, Abdulla & Smith, 2015; Ebrahim & Fattah, 2015; Zeitun & Tian, 2007).

The other reason could also be related to the inconsistent results of the previous studies about the corporate governance practices of banks in Ethiopia.

Lastly, this research aims at assessing both the corporate governance practices and its impact on the bank financial performances and with a focus on one of the private banks in Ethiopia, Zemen Bank Share Company. Most of the previous research conducted on the Government owned banks including Commercial Bank of Ethiopia and Construction Bank of Ethiopia focusing only on the assessment of the corporate governance practices.

To this effect, this study on assessments of the Corporate Governance practices in one of the private banks in Ethiopia is impressing as its findings will help Board of directors, bank managers, bank supervisors, and regulators to frame policies.

In the view of the above all, the study contributes its share to the literature in general for Corporate Governance practices and specifically for the development of the private banking sector in Ethiopia. It tries to identify the best Corporate Governance practices that can contribute for the profitability of private commercial banks.

### **1.3. Statement of the problem**

The essence of the corporate world lies in promoting transparency and accountability and in fulfilling the fair expectations of all the stakeholders. Corporate governance is one such tool to achieve this goal and to safeguard the interests of various stakeholder groups. It involves promoting the compliance of law in letter and spirit and demonstrating ethical conduct. The framework of corporate governance encourages efficient use of resources and requires accountability for the stewardship of those resources. The three key constituents of corporate governance are - Shareholders, Board of Directors and Management (Priyanka, 2013).

Corporate Governance rating services in developing countries especially in Ethiopia is scarce, if not none. It is difficult for investors and even for shareholders in Ethiopia to know the corporate governance status of any companies. Corporate Governance Rating (CGR) is an opinion on relative standing of an entity regarding adoption of corporate governance practices. In Ethiopia it is difficult for stakeholders to get information about the corporate governance practices of their entity.

Shareholders and investors need to get an independent and credible assessment result about the quality and status of their company corporate governance. This important governance rating information would help shareholders and stakeholders to determine the relative standing of the entity vis-à-vis the best practices followed in the domestic as well as international arena.

In the current actual situation on the ground and practical experiences, shareholders and investors of the banks know the corporate governance practices of their banks from the directors briefing during the annual shareholders meeting or the bank's annual report or if there is any research paper conducted by some academicians.

It is difficult even to get information about the corporate performance rating of any Ethiopian companies from internet that was rated by other international companies. Nowadays it is easy to know the corporate performance status of other African companies including Kenya banks through internet browsing. However, it is difficult to get about Ethiopian Companies including the commercial banks in Ethiopian.

Private banks in Ethiopia are expected to operate under the framework of corporate governance. There is, however, lack of strong systems to ensure compliance with principles of corporate governance. Ethiopia has no stock exchange markets but the recently established domestic private banks have been selling shares in the market, without having an institutional framework that safeguards the interest of the shareholders, which calls for the need for appropriate corporate governance.

In Ethiopia, the Corporate governance practice is at its early stage of development. All stake holders including academician and student researchers must play their own role to increase the public awareness and also advance the importance of corporate governance to the business community and the government.

A study of corporate governance practices of private banks in Ethiopia is important. In one of the studies, Bhasa, (2004) suggested that countries should develop corporate governance models unique to their needs by understanding their contextual situations. The studies made on different aspects of corporate governance largely have focused more on developed economies than emerging economies (Pamburai, Chamisa, Abdulla & Smith, 2015; Ebrahim & Fattah, 2015; Zeitun & Tian, 2007).

According to Adegbite (2012), corporate governance model and corporate behaviour are influenced by countries' institutional arrangements implying that corporate governance regulations should be considered from the context of any particular nation.

The empirical findings of studies made in developed economies might have limited application and meaning in emerging economies due to the differences in contextual settings that include organizational and environmental characteristics (Kumar & Zatonni, 2013).

The study of the state of corporate governance is very important in emerging economies like Ethiopia because of the differences in the social set up, cultural values and economic conditions compared to developed economies (Tsegabirhan, 2015). The need for effective corporate governance practice has become an important issue of discussion in Ethiopia banking industry. The concerns on the whole have started to focus on the effective protection of shareholders and investors, the promotion of transparency of board room and the banking operations, accountability, and the need for banks to move towards standardized corporate governance practices.

According to Onakoya et al. (2012) corporate governance is about building credibility, ensuring transparency and accountability as well maintaining an effective channel of information disclosure that fosters good corporate performance.

The transparency of board room and the banking operations is the issues in the banking industry. Clear accountability and transparency are becoming the core problem in the bank industry. The major issues and complaints in the private banking industry are more linked to:

- ✓ The board members' selection and appointments.
- ✓ Board members' relationship with the top bank managements.

This research aims to assess the corporate governance practices of Zemen bank, as sample cases to examines the practices and impacts of corporate governance on the bank financial performance (ROA).

The researcher aims to assess the corporate governance practices and outlines the unique features in the practices. This helps to identify the relevant gap about the corporate governance practices in the Ethiopia and particularly in the private banking sector by addressing the contextual situation. On the bases of the problems stated above, the research answers the questions below.

#### **1.4. Research Questions**

The main question that guides this research is: How does the corporate governance practices of Zemen bank which involves internal corporate governance mechanisms assessed and impact on the financial performance of the bank?

The sub questions formulated to operationalize the main research question are basically summarized into two and include:

1. How does the Internal corporate governance mechanisms of the bank board room structured and function including board size, board diversity, Board sub-committees, Board members educational qualifications and number of board meetings?
2. How does the bank board room functioning and governance variable impact the financial performance of the bank by using financial ratios including Return on Asset (ROA)?

## **1.5. Research Hypothesis**

The following are hypotheses developed to be tested in this study:

H1: There is a statistical impact of Board size on Bank Financial Performance (ROA).

H0: There is no a statistical impact of Board size on Bank Financial Performance(ROA).

H2: There is a statistical impact of Board diversity on Bank Financial Performance (ROA).

H0: There is no a statistical impact of Board diversity on Bank Financial Performance(ROA).

H3: There is a statistical impact of Board sub-committees on Bank Financial Performance(ROA).

H0: There is no a statistical impact of Board sub-committees on Bank Financial Performance(ROA).

H4: There is a statistical impact of Board members' educational qualification on Bank Financial Performance (ROA).

H0: There is no a statistical impact of Board members' educational qualification on Bank Financial Performance (ROA).

H5: There is a statistical impact of the number of Board Meetings on Bank financial performance (ROA).

H0: There is no a statistical impact of the number of Board Meetings on Bank financial performance (ROA).

## **1.6. Objective of the study**

### **1.6.1. General Objective of the study**

The main objective of the study is to assess the corporate governance practices and its impact on the financial performance of Zemen Bank Share Company.

### **1.6.2. Specific Objectives of the study**

Specifically, the research seeks to:

- ✓ Assess the impact of Bank corporate governance practices on the financial performance of the Zemen Bank specifically on the Return on Asset (ROA).
- ✓ Analyse the internal corporate governance practices of Zemen bank focusing on different aspects of corporate governance variables including board size, board diversity, Board sub-committees, Board members educational qualifications and number of board meetings and its impact on the bank performance.
- ✓ Examine board role and governance practices based on some characteristics that describe an effective Board and strategic roles.
- ✓ Examine Directors role, commitment, and their focus on the best interests of the organization and shareholders,
- ✓ Examine the major strengths of the Board and identify areas how the effectiveness of the Board can be improved and headed in the right direction as per the National Bank of Ethiopia directives.
- ✓ Assess the implementation level of corporate governance in the bank.

This research firstly performs a critical review of the literature to identify the strengths and weaknesses of the previous work in this area and secondly engaging in empirical investigation of the relationship. For the empirical part, this research thesis has used some published data and information and engaged in primary data collection. The questionnaire used to construct measures of corporate governance that are subsequently used in the empirical investigation.

### **1.7. Significance of the Study**

This study contributes its share to the literature in general for Corporate Governance practices and specifically for the development of the private banking sector in Ethiopia. It identifies the best Corporate Governance practices that can contribute for effective financial performance of private commercial banks.

The research examines the existing corporate governance practices according to the National Bank of Ethiopia (NBE) and internationally accepted organizations (OECD Principles, the Basel guidelines, Cadbury Committee deadline and other Corporate Governance best

practices). It forwards recommendations and best practices that improve the current practices. Thus, this provides the incentive for other student researcher to aim to contribute and narrow the knowledge gap in this area.

As per the knowledge of the student researcher and as shareholder of the bank, the bank did not conduct any Corporate Governance Rating by external rating company or from other professional firm about the status of Zemen bank corporate governance practices. Hence, this study conducts an independent and credible assessment of the bank corporate governance practices. The study comes up with information that benefits the shareholders and other stakeholders for their future investment decision. It helps shareholders to manage their shareholding in the bank as they can differentiate the status of the bank based on the bank corporate governance practices.

The focus of the study is on one of the private commercial banks to assess the Corporate Governance practices and its impact on the financial performances. There is limited knowledge about the corporate governance practices in the private bank sectors in Ethiopia and inconsistent results of the previous studies on the corporate governance practices and its impact on the performance of banks in Ethiopia. Hence, this research finding helps Board of directors, bank managers, bank supervisors, and regulators to frame policies.

This research can also establish the necessary groundwork and serve as benchmark for similar research in the future in the banking industry and financial sector in the country.

As mentioned in the rationale of the study, a driving force for this research, much work has not been done on corporate governance in Ethiopia (Kiyota, Peitsch & Stern, 2008). To date, the studies made on different aspects of corporate governance largely have focused more on developed economies than emerging economies (Pamburai, Chamisa, Abdulla & Smith, 2015; Ebrahim & Fattah, 2015; Zeitun & Tian, 2007).

The study which focuses on the corporate governance practice in Ethiopia and particularly on the private commercial bank is very important as there are differences in the social set up, cultural values and economic conditions compared to developed economies.

This study, therefore, contributes its share to the literature in general for Corporate Governance practices and specifically for the development of the private banking sector in

Ethiopia. It tries to identify the best Corporate Governance practices that can contribute for the profitability of private commercial banks.

### **1.8. Scope of the Study**

This research focuses on one of the private commercial banks operating in Ethiopia, Zemen Bank S.C, to assess the Corporate Governance practices and its impact on the financial performances.

For this study, descriptive research design adopted that include questionnaires, observation method and interviews. A survey of the board leaders is undertaken to see the relationships between governance structure and process with the board performances. The other survey of stakeholders' perceptions is carried out in order to scan the present status of corporate governance practices in the Zemen Bank Share Company.

Primary data obtained by distributing questionnaires to the board directors, board secretary, board sub-committee and top management. Questionnaires for board of directors collected during the monthly board meeting. The questionnaires and interview results triangulated to come up with the best research findings.

In measuring the performances, in accounting terms, secondary data obtained from the bank annual reports are considered. The study used structured review of documents, and Zemen bank financial data for ten years were collected covering a period 2010 to 2019.

The researcher examines the bank's annual reports, Charter of Boards of Directors and Sub Committees. The study reviews the National Bank of Ethiopia Directives and various documents of the Organization for Economic Co-Operation & Development (OECD), the Basel guidelines, Cadbury Committee guidelines and other Corporate Governance best practices to address various Corporate Governance related issues in details & its impact on the overall performance of the banks.

As the research focuses on the corporate governance practices of the bank, most of the information obtained from the bank's board of directors, board secretary and senior management located at their head offices.

Data collected from the Zemen bank board members, Board secretary and top management groups with Census method. Based on the permission obtained from bank board and management offices, data collected via a paper-based survey questionnaire & interview.

To name the other sources of data used include: Articles, Books, and Websites of the bank, Magazine journals, Annual reports issued in the Banking Sector and the annual reports disclosed by the National Banks of Ethiopia (NBE).

In addition to the above, the search engines such as Google, Yahoo, and Bing were effective for a wider range of information from various groups of research specialists in contributing and sharing their knowledge relating to the topic. Besides that, e-journals were found to serve as references to the study.

## **CHAPTER TWO**

### **LITRATURE REVIEW**

#### **2.1. Introduction**

The literature review of the study has two parts: theoretical and empirical literature review. The theoretical review defines corporate governance and attempts to give insight about the history of Corporate Governance concept, the corporate governance theories, corporate governance best practices, corporate governance mechanisms and review of empirical literature on corporate governance mechanisms and hypotheses developments. In the empirical literatures part, the study tried to show past study findings related to internal corporate governance mechanisms.

#### **2.2. Theoretical Literature Review**

The concept “Corporate Governance” has attracted various definitions. Although the term corporate governance is used quite ‘liberally’ now adays. It is known to mean different things to different authors. A simple search by one of the popular search engines (google) produced 424,000,000 results when it was browsed on January 2020.

The OECD is an inter-governmental body that is dedicated to sound practices for economic development. It provides an international perspective on the definition of governance. The OECD Principles of Corporate Governance (2004) states that ‘Corporate governance involves a set of relationships between a company’s management, its board, 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.’

Despite such growing interest in the subject of corporate governance (Tricker, 2009), there is no universally agreed definition of the term though the various extant definitions reflect the same basic idea. The following definitions help to establish some common understanding of corporate governance.

Nonetheless, the following definitions should give a general idea about the Corporate Governance concept: “Corporate governance deals with the ways suppliers of finance to

corporations assure themselves of getting a return on their investment” (Shleifer & Vishny 1997, p. 737).

As per the Oman (2001) broad definition, Corporate governance refers to the private and public institutions, including laws, regulations, and accepted business practices, which together govern the relationship, in a market economy, between corporate managers and entrepreneurs (corporate insiders) on one hand, and those who invest resources in corporations, on the other.

According to the Mehran (2003) definition summarized on page 1, “The term corporate governance’ essentially refers to the relationships among management, the board of directors, shareholders, and other stakeholders in a company. These relationships provide a framework within which corporate objectives are set and performance is monitored” (Mehran 2003, p.1).

As per the definition of Fernando, corporate governance differs from corporate management. As Fernando notes, corporate governance is not just corporate management; it is something much broader to include a fair, efficient, and transparent administration to meet certain well-defined objectives. It is structuring, operating, and controlling a company with a view to achieving long term strategic goals to satisfy shareholders, creditors, employees, customers and suppliers and to comply with the legal and regulatory requirements, apart from meeting environmental and local community needs (Fernando, 2009).

A more comprehensive definition of corporate governance is also provided by Rezaee (2009) as “the process affected by a set of legislative, regulatory, legal, market mechanisms, listing standards, best practices, and efforts of all corporate governance participants, including the company’s directors, officers, auditors, legal counsel, and financial advisors, which creates a system of checks and balances with the goal of creating and enhancing enduring and sustainable shareholder value, while protecting the interests of other stakeholders” .

Keasy et al. (1997) have identified the inconsistent use of the term ‘corporate governance’ by different writers and were unable to find any real consensus on the definition. According to Rose (2007) the lack of consensus in defining most of the issues surrounding corporate governance has provided a fertile ground for the growth of a Corporate Governance Industry in the United States.

### **2.2.1. Corporate Governance and the Board of Directors**

Corporate Governance is the system of rules, practices, and processes by which a firm is directed and controlled. Corporate governance essentially involves balancing the interests of a company's many stakeholders, such as shareholders, senior management executives, customers, suppliers, financiers, the government, and the community (James, 2020).

As stated by Jame (2020), the board of directors is the primary direct stakeholder influencing corporate governance. Directors are elected by shareholders or appointed by other board members, and they represent shareholders of the company. The board is tasked with making important decisions, such as corporate officer appointments, executive compensation, and dividend policy. In some instances, board obligations stretch beyond financial optimization, as when shareholder resolutions call for certain social or environmental concerns to be prioritized.

A company's board of directors is the primary force influencing corporate governance. Governance is “everybody’s job.” However, the key governance responsibilities are typically entrusted to the board of directors and the executive management of a corporation who are responsible for providing the oversight that is intended to help ensure that a company meets its goals (Levine, 2004).

### **2.2.2. History of Corporate Governance**

As stated by Tsegabirhan (2015), the concept of corporate governance can be traced back to the 18th century.

The importance of corporate governance became dramatically clear at the beginning of the twenty-first century as a series of corporate meltdowns arising from managerial fraud, misconduct, and negligence caused a massive loss of shareholder wealth. The firm’s owners (shareholders) asked who, if anybody, is responsible for protecting and promoting the value of their investment. Yet governance issues and problems have a long and sometimes shocking history. Adam Smith (1776) wrote in *Wealth of Nations*:

*Being the managers of other people’s money rather than their own, it cannot be expected that they [managers] should watch over it with the same anxious vigilance which [they would] watch over their own. Negligence and profusion,*

*therefore, must always prevail, more or less, in the management of the affairs of such a company.*

Corporate governance emerged to be very important when many interested individuals and groups raised and merged their capital in order to finance huge enterprises. With the establishment of such enterprises comes the question of their management and control since the multiple owners cannot manage and control the business they own. This gap has to be filled by an appropriate organ that functions in the best interests of the owners, justifying the need for corporate governance (Said, Jaafar & Atan, 2015; Tricker, 2009; Bainbridge, 2008; Garg, 2007; Wearing, 2005; Okeahalam & Akinboade, 2003; Blair, 1995). Three decades ago, the term corporate governance meant little to all but a handful of academics. Today, it is a mainstream concern. Several events are responsible for the keen interest in corporate governance. International attempts at reforming corporate governance have been preceded by well-publicized cases of major corporate collapse in a number of developed economies in the 1980s, especially in the UK and US (Barrier, 2003; Mallin, 2007).

The consensus was that poor corporate governance practices played a pivotal role in causing these corporate failures (Cadbury Report, 1992; Jones & Pollitt, 2004).

### **2.2.3. Corporate Governance in Africa**

Corporate governance has existed for centuries and has taken a stronger foothold in developed economies when compared to emerging economies. However, African economies began to pay particular attention to the ideals of good governance in the beginning of the 1980s. According to Soyibo, et al (2002), the term good governance was first mentioned in a 1989 World Bank report on Sub-Saharan Africa but since the 1990s many donor agencies have sought the pursuit of good governance (Ayandele & Isichei, 2013).

There is little research on corporate governance in Africa (Negash, 2008; Economic Commission for Africa (ECA), 2005; Okeahalam & Akinboade, 2003). The limited studies are dominated by commission reports<sup>1</sup>, and hence, well-grounded studies are scarce, and this is especially true regarding the Sub Saharan Africa context. In Africa, the numbers of listed companies are few and most of them are family or small private enterprises and state-owned corporations that are characterized by weak regulatory and supervisory framework (Okeahalam & Akinboade, 2003; Armstrong, 2003; ECA, 2005).

Until the 1980s, African economies were largely state-controlled. In economic terms, state control was reflected in the following: (1) The predominance of state-owned enterprises in all sectors of the economy; (2) the administrative control of interest rates and credit allocation to companies and various sectors of the economy; and (3) exchange rate controls. Concomitant with the state-controlled economy was the lack of a democratic culture and institutions. For many African countries, dictatorship by either military or civilian governments was the order of the day. The traditions of rule of law, transparency, accountability, and social justice, which underpin governance, both at the national and corporate levels were non-existent. In State-owned Enterprises, the government appoints the directors or managers who make day-to-day decisions about the enterprise and exercise property rights. Through the directors the government made decisions regarding investment, production, procurement, and personnel matters. As a regulator, the government sets technical standards of products, product prices and sometimes gives directives on cross-subsidization (Otobo, 2000).

The introduction of principles and standards of corporate governance contextualized in an African way is important (Economic Commission for Africa, 2005). Some African countries have recently started to introduce reform measures with corporate governance that has led to the establishment of corporate governance codes in Ghana, Uganda, Kenya, Tanzania, Zambia, Malawi, Zimbabwe, Mauritius, and others. What is lacking according to Armstrong (2003), however, is the regulatory and institutional framework that will enforce these standards in the countries concerned.

According to Africa's corporate governance network (ACGN) research conducted in 13 countries on February 2016, the implementation of corporate governance is at different stages of progress. South Africa is most advanced in this regard followed by Mauritius, Kenya, and Nigeria. Uganda and Zambia have shown good progress while Zimbabwe is regressing (ECA, 2005).

#### **2.2.4. Corporate Governance in Ethiopia**

Roberston (2009) and Negash (2008) as quoted in Tsegabirhan (2015), Since the regime change from a Military Government to a Transitional Government in 1991, Ethiopia has launched a series of economic adjustment and reform programs geared towards building a competitive private sector. This set of reforms has increased the size and role of the private sector. Even though the economy is dominated by smallholder agricultural activities, over the

last two decades, the number of corporate forms of business firms has increased due to the liberalization of the economy. This development has increased the awareness and importance of corporate governance and drawn much attention to guarantee the protection of investors' interests and thereby encourage and boost investment.

The history of the establishment of share companies in Ethiopia dates to 1960 during the Imperial regime and became routine between 1960 and 1973. For the first time it was in 1960 that the legal framework for corporate governance was laid when the two legal institutions, Commercial Code and Civil Code, were proclaimed (Negash, 2008).

Ethiopia has no stock exchange markets but the recently established domestic private banks have been selling shares in the market, without having an institutional framework that safeguards the interest of the shareholders, which calls for the need for appropriate corporate governance. Private Banks are expected to operate under the framework of corporate governance. There is however, lack of strong systems to ensure compliance with principles of corporate governance (Tsegabirhan, 2015).

According to Kefale (2019), Ethiopia has no separate corporate governance regulation, rather corporate governance issues are covered under the company law part of the 1960 Ethiopian commercial code. The Ethiopian commercial code has not been amended since 1960 and with the new corporate practice trend; the corporate governance provisions are not modern and progressive to answer sophisticated governance issues. Apart from its obsolescence, corporate governance issues are not covered holistically under the commercial code and many corporate issues remain unanswered.

Corporate governance is at its infancy stage in Ethiopia; absence of comprehensive company law coupled with the obsolescence and inadequacy of the commercial code legislative provisions, which was enacted in 1960 are the basic reasons for poor corporate governance in Ethiopia. Accordingly, the commercial code does not have adequate legislative provisions on governance issues related to the separation of supervision and management responsibilities, and on the composition, independence, and remuneration of board of directors in companies (Hussien, 2012).

Ethiopia is at a critical time to answer an ever-growing demand of wealth distribution among the general public. Establishment of big share Companies which are open to the public is the

basic mechanism of creating wealth and distributing it which will solve public questions. However, it is necessary to have an efficient corporate structure so that the wider public will have confidence to invest its money in such companies. People worry about the return of their investment before they purchase shares, and the main source of their worries is the trustworthiness and efficiency of the corporate management (Kefale, 2019).

### **2.2.5. Goals of Corporate Governance**

According to Benton (2007), one model of corporate governance does not fit all users; that there are international differences; and that corporate governance has multiple goals. These goals include but are not limited to protecting shareholders' interests; protecting stakeholders' interests; protecting the public's interest in the banking system; and satisfying bank/government regulators. Because there are different goals, investors, regulators, and stakeholders have different measures of success or failure. Some of the measures may be tied to laws and regulations that affect the structure of corporate governance. Some of the measures involve the following issues: effectiveness and efficiency of operations, reliability of financial reporting, compliance with laws and regulations, returns on investments; and achieving stakeholders' goals.

### **2.2.6. Corporate Governance Best Practices**

Corporate governance best practices offer guidelines for board members to be most effective in bringing strategic value to their organizations. Board chairpersons and members help ensure the board plays a key role in their company's success when they develop strong understanding of, and successfully implement, corporate governance best practices.

### **Cadbury Committee**

The Committee on the Financial Aspects of Corporate Governance, forever after known as the Cadbury Committee, was established in May 1991 by the Financial Reporting Council, the London Stock Exchange, and the accountancy profession. The spur for the Committee's creation was an increasing lack of investor confidence in the honesty and accountability of listed companies, occasioned by the sudden financial collapses of two companies, wallpaper group Coloroll and Asil Nadir's Polly Peck consortium: neither of these sudden failures was at all foreshadowed in their apparently healthy published accounts.

The Cadbury Committee published the “Code of Best Practice” to analyze the effectiveness of UK board. The Cadbury Committee was appointed by the UK government in 1992. The code is a voluntary code based on “comply or explain” approach of implementation. That is, listed companies in the London Stock Exchange are required to state whether they are complying with the code or explain for their non-compliance. The Code recommends that publicly listed companies should have at least three outside directors and that the position of the chairman of the board and chief executive officer (CEO) should not be held by the same person. They find that CEO turnover increased after the publication of the code and that the relationship between CEO turnover and performance was strengthened (Cadbury Committee, 1992).

### **Basel Guidelines**

According to the Basel Committee on Banking Supervision (2013), the Basel Committee - initially named the Committee on Banking Regulations and Supervisory Practices - was established by the central bank Governors of the Group of Ten countries at the end of 1974 in the aftermath of serious disturbances in international currency and banking markets (notably the failure of Bankhaus Herstatt in West Germany). The Committee, headquartered at the Bank for International Settlements in Basel, was established to enhance financial stability by improving the quality of banking supervision worldwide, and to serve as a forum for regular cooperation between its member countries on banking supervisory matters. Since its inception, the Basel Committee has expanded its membership from the G10 to 45 institutions from 28 jurisdictions. Starting with the Basel Concordat, first issued in 1975 and revised several times since, the Committee has established a series of international standards for bank regulation, most notably its landmark publications of the accords on capital adequacy which are commonly known as Basel I, Basel II and, most recently, Basel III.

### **Basel I: The Basel Capital Accord**

With the foundations for supervision of internationally active banks laid, capital adequacy soon became the focus of the Committee's activities. Backed by the G10 Governors, Committee members resolved to halt the erosion of capital standards in their banking systems and to work towards greater convergence in the measurement of capital adequacy. This resulted in a broad consensus on a weighted approach to the measurement of risk, both on and off banks' balance sheets.

## **Basel II: The new capital framework**

In June 1999, the Committee issued a proposal for a new capital adequacy framework to replace the 1988 Accord. This led to the release of a revised capital framework in June 2004. Generally known as "Basel II", the revised framework comprised three pillars:

1. minimum capital requirements, which sought to develop and expand the standardized rules set out in the 1988 Accord
2. supervisory review of an institution's capital adequacy and internal assessment process
3. effective use of disclosure as a lever to strengthen market discipline and encourage sound banking practices

## **Basel III: responding to the 2007-09 financial crisis**

Even before Lehman Brothers collapsed in September 2008, the need for a fundamental strengthening of the Basel II framework had become apparent. The banking sector entered the financial crisis with too much leverage and inadequate liquidity buffers. These weaknesses were accompanied by poor governance and risk management, as well as inappropriate incentive structures. The dangerous combination of these factors was demonstrated by the mispricing of credit and liquidity risks, and excess credit growth.

The provisions that came in by the way of Basel guidelines relate to risk management in banks. There is a strong practical reason for interpreting bank reports to be adjusted for the different riskiness of the assets reported by a bank for public information. In a sense, good corporate governance dictates that the bank management must practice good governance in knowing the risk-adjusted size of their reported assets. Hence, any adoption of Basel recommendations should also be looked at as part of corporate governance, not simply as good reporting practice (Ariff and Hoque 2007).

The Basel Committee's guidance draws from principles of corporate governance published by the Organization for Economic Co-operation and Development (OECD). The OECD's widely accepted and long-established principles aim to assist governments in their efforts to evaluate and improve their frameworks for corporate governance and to provide guidance for participants and regulators of financial markets.

### **2.2.7. OECD Principles of Corporate Governance**

OECD principles of corporate governance were first introduced in 1999 and since then have become a benchmark example of the best industry practices. Principles have been regularly reviewed since 1999 in order to address the real-world experiences that OECD and non-OECD companies face. The last revision of these principles occurred in 2004(OECD2004). These principles do not offer a single ideal model of corporate governance for publicly traded companies. Instead, the principles suggest a path that could eventually lead to the formation of good corporate governance in any organization and consequently help the organization to operate more efficiently, lower the costs of the capital, and stimulate growth.

The principles were developed and endorsed by the ministers of OECD member countries in order to help OECD and Non-OECD governments in their efforts to create legal and regulatory frameworks for corporate governance in their countries. The OECD is an international body formed by 34 developed countries to produce a set of globally accepted principles of corporate governance.

The six OECD Principles are ensuring the basis of an effective corporate governance framework, the rights of shareholders and key ownership functions, the equitable treatment of shareholders, the role of stakeholders in corporate governance, disclosure and transparency and the responsibilities of the board (OECD2004):

#### **-Ensure the basis of an effective corporate governance framework**

The corporate governance framework should promote transparent and efficient markets, be consistent with the rule of law and clearly articulate the division of responsibilities among different supervisory, regulatory and enforcement authorities.

#### **-The rights of shareholders and key ownership functions**

The corporate governance framework should protect and facilitate the exercise of shareholders' rights. This is one of the basic rights that states that the corporate governance framework should protect and aid the exercise of shareholders' rights. Shareholders have the right to vote, thus, corporate governance should ensure that there is one vote for one share. It ensures that shareholders have the right to vote in absentia if they cannot be present

physically; should have the right for authorization of additional shares and should have the right to ask questions.

### **-The equitable treatment of shareholders**

The corporate governance framework should ensure the equitable treatment of all shareholders, including minority and foreign shareholders. All shareholders should have the opportunity to obtain effective redress for violation of their rights. A corporate governance framework should ensure equitable treatment of all shareholders in the same series of classes. It should ensure the same voting rights and equal treatment of shareholders within the same class of shares. The principles also state that:

- All shareholders of the same series of a class should be treated equally
- Insider trading and abusive self-dealing should be prohibited
- Members of the board and key executives should be required to disclose to the board whether they, directly, indirectly or on behalf of third parties, have a material interest in any transaction or matter directly affecting the corporation.

### **-The role of stakeholders in corporate governance**

The corporate governance framework should recognize the rights of stakeholders established by law or through mutual agreements and encourage active co-operation between corporations and stakeholders in creating wealth, jobs, and the sustainability of financially sound enterprises. Corporate governance should ensure that these rights are respected. It should acknowledge that relationship with stakeholders is important for building sustainable enterprises and mutual development by fostering teamwork. Therefore, corporations should recognize the contributions of stakeholders for the long-term success of the corporation and should always take into account their interests in taking decisions and actions.

### **-Disclosure and transparency**

The corporate governance framework should ensure that timely and accurate disclosure is made on all material matters regarding the corporation, including the financial situation, performance, ownership, and governance of the company. The corporate governance framework ensures transparency and disclosure of material information on a timely and accurate basis concerning the financial situation, operating performance, annual audit, and

governance structure and policy, board and management members, and objectives of the company.

### **-The responsibilities of the board**

The corporate governance framework should ensure the strategic guidance of the company, the effective monitoring of management by the board, and the board's accountability to the company and the shareholders. The principle specifically states that boards have the responsibility to act on informed basis, in good faith, with due care and in the best interests of the company and the shareholders. The board has also the responsibility to consider the interests of stakeholders in its decisions and actions. In general board members should be able to commit themselves effectively to the responsibilities entrusted to them.

#### **2.2.8. The 2009 King Report on Corporate Governance for South Africa (KING III)**

The third report on governance in South Africa (King III) became necessary because of the anticipated changes in international corporate governance trends. The following subsections examine the origin and the internal corporate governance structures imposed by the 2009 King Report on Corporate Governance for South Africa.

King III is based on an “apply or explain” basis in contrast to King II & I. The main reason for the shift from “comply or explain” to “apply or explain” was the application of the reports. King II was drafted considering affected entities and included listed companies, financial institutions, and public entities (Institute of Directors in Southern Africa, 2009:11).

#### **2.2.9. Laws and Directives on Corporate Governance of banks in Ethiopia**

Publicly held companies are referred to as “share companies” in Ethiopia's Commercial Code. Even though all companies (including financial institutions) have to adhere to the provisions of the Commercial Code to operate in the country, financial companies have other proclamations and subsidiary directives that require them to comply with additional requirements (USAID, 007).

According to Husen (2012), Share companies engaged in banking have to comply with the Banking Business Proclamation No.592/2008 and the directives and procedures issued by the

National Bank of Ethiopia (NBE). This specifies laws apply to financial share companies in addition to the Commercial Code.

### **Ethiopia's Commercial Code**

The definition of “director” is nowhere given under the Commercial Code of Ethiopia. The term is defined under Article 2(6) of the Banking Business Proclamation No. 592/2008 as “any member of the board of directors of a bank, by whatever title he may be referred to.” In this definition, the important factor to determine whether a person is a director is to refer to the nature of the office and its duties. It does not matter by what title s/he is referred to. If s/he is the member of the board and performs the functions of a directorship, s/he would be considered as a director in the eyes of the law (Husen, 2012).

According to Husen 2012, there is a unitary board of directors in share companies in Ethiopia. The law does not distinguish between managerial and supervisory roles of the board. The Commercial Code provides that the board of directors shall appoint a manager and that only members may be appointed as directors.

Article 14(4)(c) of the Banking Business Proclamation No.592/2008 provides that the National Bank may issue directives on the duties, responsibilities, and good corporate governance of board of directors.

The Commercial Code of Ethiopia (1960) has provisions on corporate governance application. The part which is related to share companies is Articles 304-428, where shares and rights and duties of shareholders, directors, auditors, and shareholder meetings are clearly stipulated. Summary of the provision may include the following:

#### **2.2.10. National Bank of Ethiopia Corporate Governance Directives**

Corporate governance plays a vital role in maintaining the safety and soundness of financial system in general and banking sector in Ethiopia in particular. The National Bank of Ethiopia (NBE) issues different Directives to provide guidelines to ensure banks are soundly and prudently managed and directed.

As per the financial directives for Bank Corporate Governance, “Corporate governance” means the process and structure used to direct and manage the business and affairs of a bank

towards enhancing business prosperity and corporate accountability with ultimate objectives of realizing long term shareholders' value as well as customers and other stakeholders' interest (Bank Corporate Governance, 2019).

The following is the summary for some of the NBE directives

**A) Board Size and composition**

As per the National Bank of Ethiopia Directive, a bank shall have at least nine directors. The board may preferably comprise of directors who as a group provide a mixture of core competencies such as banking, finance, accounting, management, economics, legal, business administration, auditing information technology and investment management. The board shall comprise of female directors provided that eligible candidates are available among the shareholders. The board of Bank shall comprise minority shareholders (Bank Corporate Governance, 2019).

**B) General meeting of Shareholders**

According NBE directive, the ordinary general meeting of shareholders of a bank shall strive in a good faith that only competent and reliable persons who can enrich good corporate governance and add value to the bank are elected or appointed as a director without prejudice to the provisions in the Commercial Code of Ethiopia. The directive also stated that the General meeting of shareholders to ensure that the board is held accountable and responsible for the inefficient and ineffective governance (Bank Corporate Governance, 2019).

**C) Knowledge, Experience and Age**

According to NBE directive, the nominated candidates to the board of a bank shall meet knowledge, experience and age requirements, directors, a chief executive officer and senior executive officers shall fulfil at a minimum, the following: At least seventy five percent of a bank's board members shall hold a minimum of first degree or equivalent from recognized higher learning institution; and the remaining board members, at a minimum, shall complete general secondary school or its equivalent, member of board of directors shall have adequate experience in business management, preferably in banking business, and/or should take adequate training in banking business management after holding a seat on the board, a

director shall be at least 30 years old (Requirements for persons with Significant Influence in a Bank, 2012).

According to NBE directive, a chief executive officer shall hold a minimum of first degree from recognized higher learning institution; and have a minimum of 10 years' experience in banking, of which, at least 5 years shall be in a managerial position (Bank Corporate Governance, 2019).

#### **A) Qualifications and trainings**

As per the National Bank of Ethiopia directive, a bank shall give training to directors at least once in a year on priority basis in areas of financial analysis, corporate governance, applicable laws, regulations and directives and risk management and internal control. A bank shall file certificate of training of each member of the board to the National Bank for validation of its compliance with sub article 10.2.2 of this article (Bank Corporate Governance, 2019).

#### **B) Meetings**

As per the National Bank of Ethiopia directive, the board shall set up and put in use rules for the manner of conducting board meetings, board meetings 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 board meetings, the board shall appoint a secretary, the board shall fix regular meeting days and venue, the chairperson or the secretary of the board shall serve formal notice of meeting to each director, together with agenda items, at least three days earlier than the meeting day, a director shall attend in person at least 75% of the board meetings of a bank within the financial year. failure to do so, unless adequately justified and accepted by shareholders general meeting, will render automatic cancellation of his/her seat on the board and the proceedings of board meetings shall be minute and sequentially numbered (Bank Corporate Governance, 2019).

#### **C) Disclosures**

According to the National Bank of Ethiopia directive, board and senior management of a bank shall be transparent to any shareholder, depositor and any other relevant stakeholders without breaching the law of the country and the National Bank directives, a bank shall at a

minimum disclose the following without prejudice to provision in other laws and the national bank directives, Submit any related party loan/foreign currency transactions, banks fixed assets, and technology transactions of material nature as defined by the board, to the National Bank within fifteen days from the date of transaction (Bank Corporate Governance, 2019).

As per the National Bank of Ethiopia directive, the annual board compensation to a director shall not exceed Birr 150,000. The sub articles also stated that the monthly allowance paid to a director shall not exceed Birr 10,000, no employee of a bank be it permanent or contractual, shall sit on the board of any bank and no bank shall pay any financial or otherwise remuneration or benefits other than those stated under the above sub articles of this article in whatsoever form to its directors any time (Limits on Board Remuneration and Number of Employees Who Sit on a Bank Board, 2018).

The National Bank of Ethiopia directive also states that the board should at a minimum set-up the following sub-committees:

- **Audit sub-Committee**

to provide independent oversight of the bank's financial reporting and internal control system and ensuring checks and balances within the bank, the Audit sub-Committee shall comprise at least three directors. At least one member should have accounting or auditing expertise or experience in the field of finance, the Audit sub-Committee should have explicit authority to investigate any matter within its terms of reference, full access to and co-operation by management and full discretion to invite any director or executive officer to attend its meetings, and reasonable resources to enable it to discharge its functions properly. The Audit sub-Committee should have full and unrestricted access to information and be able to obtain independent professional advice. Duties of Audit and Compliance Committee, among others, to ensure fair and transparent reporting and prompt publication of the financial accounts; to oversee the functions of the Internal Audit Unit; to review the scope of the internal audit program , internal audit findings and recommend actions to be taken by management; to appoint, set compensation, evaluate performance and decide on the transfer and dismissal of the Chief Internal Auditor; to review the effectiveness of internal controls and risk management processes; to recommend the appointment and the removal of external auditors; to the subcommittee shall hold regular meetings, at least once every quarter and should report regularly to the full board (Bank Corporate Governance, 2019).

- **Risk management and compliance sub-committee**

According to the National Bank of Ethiopia directive issued for risk management and compliance sub-committee, to oversee senior management's activities in managing credit, market, liquidity, operational, legal and other risk and to ensure that the risk management process is in place and functioning, the Risk Management & Compliance Sub Committee should comprise at least three directors, the Risk Management & Compliance Sub Committee is responsible at least for: reviewing and recommending risk management strategies, policies and risk tolerance limits for board's approval; reviewing and assessing adequacy of risk management policies and framework in identifying, measuring, monitoring and controlling risk and the extent to which these are operating effectively; ensuring infrastructure, resources and systems are in place for risk management; ensuring that the staff responsible for implementing risk management systems perform those duties independently of the bank/insurance/MFI risk taking activities; and reviewing management's periodic reports on risk exposure, risk portfolio composition and risk management activities and the sub-committee shall hold regular meetings, at least once every quarter and should report regularly to the full board (Bank Corporate Governance, 2019).

- **Human resource affairs sub-committee**

According to the NBE directive issued for human resource affairs subcommittee, the primary objective of Human Resource Affairs Sub-Committee is to provide formal and transparent proposal on the employment and removal of senior management members if they are ineffective, errant or negligent in discharging their responsibilities and on the overall compensation/benefit system of the bank, the Human Resource Affairs Sub-Committee shall comprise at least three directors, the Human Resource Affairs Sub-Committee is responsible for recommending a framework of hiring and replacing members of senior management of the bank, recommending to the whole board on removal of the member of senior management of the company where they found to be ineffective, errant or negligent in discharging their responsibilities, recommending and monitoring of salaries and benefits for the member of senior management and overall benefit packages (bonus, salary increment, etc..) of the bank, overseeing management succession planning and performance evaluation of members of senior managements, ensuring that all Nomination and Election Committee member get training on approved" Procedure for Nomination and Election of Board of

Directors” and elected directors receive an appropriate induction and continuous training in order to keep abreast with the latest development in the industry, overseeing any major changes on the overall benefit structure of the bank; and considering disciplinary issue related to senior management members and the sub-committee shall hold regular meetings, at least once every quarter and should report regularly to the full board (Bank Corporate Governance, 2019).

### **2.3. Empirical Literature Review**

The next subsection reviews the empirical literature on the relationship between corporate governance mechanisms and company performance to develop hypotheses. Accordingly, the hypotheses on the effect of board size, board diversity, board sub-committees, Board members educational qualification and number of board meetings on financial performance are developed. These hypotheses are crafted from the combined orientations of the agency theory, resource dependence theory and stewardship theory.

#### **2.3.1. Corporate Governance Mechanisms**

Corporate governance mechanisms are means or control structures used by the principals to align the interests of principals and agents and to monitor and control agents. The purpose of these governance mechanisms is to limit the scope and frequency of agency costs and to ensure that agents act in accordance with the best interests of their principals (Gebba, 2015).

Researchers often categorize corporate governance mechanisms into two categories, i.e. internal and external corporate mechanisms. The internal mechanism is divided into five basic categories, they are: the board of commissioners (roles, structures, and incentives), managerial incentives, capital structure, constitutions and corporate regulations, and internal control system. Whereas external mechanism is divided into five categories, they are: law and regulations, market, capital market information and analysis, accounting market, finance and law, and special sources of external control (Gillan, 2006 cited in Dharmastuti & Wahyudi, 2013).

Corporate governance is divided into external and internal corporate governance. Internal corporate governance covers public’s interest, employees’ interest, and owners’ interest. While external corporate governance is defined as a mechanism through which governments’

responsibility to control the operations of banks are exercised based on the prevailing bank regulations (Ben, Patrick & Caleb, 2015).

### **2.3.2. External Governance Mechanisms**

Financial regulators and central banks devote much effort to monitoring & regulating the banking industry. Good corporate governance is not the result of only internal corporate governance mechanisms, but there are also external corporate governance mechanisms which are important in reducing the agency problem in banks. In the banking sector, the government establishes relatively higher regulation to save the interests of the depositors as well as the general public. In countries like Ethiopia, where there is no capital market, the effect of the market for corporate control on corporate governance may be minimal. Instead, the government's regulation and supervision as an external corporate governance mechanism plays major role in the governance of banks. Accordingly, external corporate governance is considered as a mechanism, which places the government's responsibility to control the operations of banks through prevailing bank regulations. Central bank regulation is exercised using various financial ratios of individual banks (Ashenafi et al, 2013).

Banking is a very important sector because the development of the finance, and particularly the banking system, promotes economic growth. Hence, it is important to control and regulate bank processes by an apex bank to ensure customers' safety, strengthen and promote soundness, stability, and efficiency of the banking system. Assessment of financial performance of the banking sector is a powerful measure and pointer to check the soundness of economic activities of an economy. Parameters are used to evaluate the operating soundness, financial performance, financial condition, and regulatory compliance of the banking organization (Ishaq et al.2016).

According to Babatunde & Olaniran (2009) cited in Razel (2017), formal legal and regulatory obligations are part of the external incentive structure designed to ensure that competing companies abide by common standards of fairness, transparency, accountability, and responsibility to protect shareholders, consumers, workers, the environment, and even competitors from abusive practices. A good legal and regulatory framework efficiently addresses the entry, operations, and exists of firms.

### **2.3.3. Internal Governance Mechanisms**

Organizations need internal mechanisms of CG to mitigate the probability of having agency problems. The agency theory is assumed to afford a foundation of CG using internal CG mechanisms. In addition, the agency theory could arrange the relationship between BoD characteristics and firm performance (Kyereboah & Biekpe; 2006).

Several characteristics of the board of directors (size, composition, or functioning) might reflect directors' motivation and their ability to effectively monitor and advise managers. Banks with boards that are more effective in monitoring and advisory terms are better governed, and that better governance creates shareholder value (Andres & Vallelado, 2008).

A well governed corporation needs to balance the roles of three groups of players: shareholders, boards of directors, and managers, while meeting all of its financial commitments and other obligations to a broad array of stakeholders. The board of directors represents the interests of shareholders and may have obligation to other stakeholders under various statutory and voluntary provisions. An independent board of directors, the core internal governance mechanism, is the bridge between management and owners, other stakeholders, and the outside world (Babatunde & Olaniran, 2009).

By bringing expertise and knowledge, the board plays an important role in formulating and implementing business strategy. The board can oblige management to justify its proposed actions and to invoke reasoned arguments to support the options it has chosen, thus, performing a monitoring function (Fernandes, Farinha, Martins, & Mateus, 2017).

There are different mechanisms embraced that defend the interests of the stakeholders. Such corporate governance mechanisms include board size, board gender diversity, and board of directors' educational qualification (Stephen, Djan, Bawuah, Halidu, & Kuutol, 2015). The effectiveness of the board is influenced by factors such as board composition and quality, size of board, board diversity, and board committee effectiveness. Agency theories suggests that corporate boards must implement various mechanisms (board composition, board size, frequency of board meeting, board committee etc.) to align the interest of opportunistic agents to shareholders interest (Puni, 2015).

As already mentioned, one of the mechanisms that shareholders rely upon is internal corporate governance mechanisms. This relates to mechanisms that are in place to ensure that agency relationship is nurtured. The variables specific to this study are board size, board diversity, board sub-committees, board members educational qualification and number of board meetings.

#### A. Board size and Bank Financial Performance(ROA)

The definition of board size is the total number of directors on a board (Levrau and Berghe, 2007). The issue of board size as a corporate governance mechanism has received considerable attention in recent years from academics, regulators and market participants. It continues to receive attention because empirical evidence of the impact of board size on company performance is inconclusive (Johl, Kaur & Cooper, 2015; Uadiale, 2010).

Board size represents number of directors on a board. Boards having too many directors could be unproductive with ineffective communication that results directors free riding problem (Alam & Akhter, 2017). While the board's capacity for monitoring increases as more directors are added, the benefit may be outweighed by the incremental cost of poorer communication and decision- making associated with larger groups (John & Lemma, 1998).

The Cadbury Committee (Cadbury, 1992) recommends an ideal board size of 8–10 members, with an equal number of executive and non-executive directors.

Brown and Caylor (2004) also suggest that a board size of between six and 15 members is ideal to enhance firm performance. Small board size was favoured to promote critical, genuine, and intellectual deliberation and involvement among members, which presumably might lead to effective corporate decision- making, monitoring and improved performance (Lawal, 2012).

Lipton and Lorsch (1992) argue that board size should be small and limited: a board size of 8–9 directors is optimal for coordination and communication, because if the board has more than 10 members, it is not easy for directors in the board to indicate their opinions and ideas. However, Dalton and Dalton (2005) argue that the advantage of larger boards is the spread of expert advice and opinions around the table compared to a small board. Larger boards are expected to increase board diversity in relation to experience, skills, gender and nationality.

Lipton and Lorsch (1992) cited in Uwuigbe and Fakile (2012) suggested that larger boards are less effective than smaller boards due to co-ordination problems in larger boards. They recommended limiting the membership of boards to ten people, with a preferred size of eight or nine. They further opined that even if boards' capacities for monitoring increases with board size, the benefits are outweighed by such costs as slower decision-making, less candid discussions of managerial performance, and bias against risk-taking.

Empirically, the researcher found that the relationship between board size and banks financial performance in the existing literature is inconclusive. There are three streams of research findings, those that report a positive impact (Adesanmi, Sanyaolu & Ngene (2018); Elbannan & Elbannan (2014) and Al-Amarneh (2014)), those that record a negative relationship (Ashenafi, Kelifa, & Yodit (2013); Rao & Kidane (2016) and Orazalin, Mohmood, & Jung Lee (2016) and those that report no association (Agyemang, Aboagye & Frimpong (2014); Yasser, Entebang & Mansor (2011:482) and Ben, Patrick & Caleb (2015)).

Adesanmi, Sanyaolu & Ngene (2018) examined the effect of corporate governance on the financial performance of banks in Nigeria from 2005 to 2014. The study found that there was a positive and significant relationship between Board Size and ROA of the studied companies in the banking sectors. Elbannan and Elbannan (2014) examine the association between governance quality and performance by estimating OLS regression models with pooled observation to test this relation. The study covered 48 sample banks in Egypt with a 10-year data. Results indicate that board size had positive impact on the bank performance.

Al-Amarneh (2014) investigated the ownership structure and corporate governance on bank performance in Jordan with sample of 13 banks for the years 2000-2012. Results indicated that board size was statistically significant and positively related to the ROA.

Ashenafi, Kelifa, & Yodit (2013) examined the internal and external corporate governance mechanisms and their impact on performance of commercial banks in the absence of organized stock exchange. Multivariate regression model was used to analyse 7-year data of 7 private and 2 state-owned Ethiopian banks. Board size is statistically significant and had negative effect on ROA. Board size had an adverse effect on performance, suggesting that banks with larger boards tend to perform poorly compared to banks with smaller boards. Adverse effect of board size on bank performance may be because boards with too many directors could be unproductive, with ineffective communication among directors in the board.

This leads to director free riding problem i.e., directors consume more resources than they contribute to the bank, and thereby reducing bank performance.

James and Joseph (2015) examined the corporate governance mechanisms specifically the ownership monitoring mechanism, internal control monitoring mechanism and regulatory mechanism influence on bank performance. Multiple regression analysis approach revealing results that board size have negative relationship with ROA.

Rao and Kidane (2016) undertook a study to determine the effect of corporate governance variables on the financial performance of commercial banks in Ethiopia. 14 banks (2 state-owned and 12 private) operational for 5 years. Panel regression model was employed. The results revealed that board size had negative effect impact on ROA.

Orazalin, Mohmood, and Jung Lee (2016) investigated the impact of different dimensions of corporate governance practices such as board characteristics (board composition, board committee, board size), ownership structure, corporate disclosure and CEO education on the operating performance of 30 Russian banks for a period covering 9 years. Results showed that board size was negatively associated with ROA.

Agyemang, Aboagye and Frimpong (2014) studied a sample of eight banking companies listed on the Ghana Stock Exchange with data from 2007 to 2012. They found that no significant relationship between board size and company performance.

Ben, Patrick and Caleb (2015) investigated the impact of corporate governance on money deposit bank performance in Nigeria with data period of 8 years. Result shows that the board size had no differential effect on banks' performance.

As per the National Bank of Ethiopia Bank Corporate Governance Directive, a bank shall have at least nine directors. While the Ethiopian commercial code Article 347 mandated a company to have not less than three nor more than twelve directors who shall form a board of directors. The National bank of Ethiopia does not specify the exact number of directors that should form a board, but it does set out a general principle that every board must consider that make the board effective. This suggests that a company's board size may affect its performance and hence it allows companies to determine the actual board size (Bank Corporate Governance, 2019).

Given the gap in predicting the exact number of board of directors and the relationship between board size and bank performance, the first pair of hypotheses for the study is proposed as follows:

***H<sub>10</sub>: There is no statistically significant relationship between board size and bank financial performance (ROA).***

***H<sub>1a</sub>: There is a statistically significant positive relationship between board size and bank financial performance (ROA).***

#### **B. Board diversity and Bank Financial Performance(ROA)**

A board of directors is an essential mechanism that can enhance and create the coalitions with the stakeholders controlling resources required by a firm (Westphal and Milton,2000). Each director brings a collection of unique and different experiences, attachments, and points of view to a board (Wang and Dewhirst, 1992). Several studies suggest a diversified and well-balanced board of directors can significantly enhance a firm's performance.

Board diversity is broadly defined as various attributes, such as age, gender, ethnicity, culture, religion, constituency representation, independence, knowledge, educational and professional background, technical skills and expertise, commercial and industry experience, and career and life experience (Van der Walt & Ingley, 2003).

According to Adams and Mehran (2003) cited in Fernandes et al. (2017) the rationale behind the view of diversity as a positive force within boards builds on the assumption that the existence of multiple and divergent viewpoints within a board will decrease the likelihood that the agenda and initiatives will be dominated by management thus improving the monitoring role of the board.

According to the citation made by Johannes (2017) about the different researchers' views that were categorized as proponent and opponent of board diversity are described as follows:

Proponents of diversity in corporate boardrooms usually base their arguments on agency, resource dependence, human capital and signalling theories (Taljaard et al., 2015). First, the agency theory states that diversity in the boardroom increases board independence and improves executive monitoring (Van der Walt & Ingley, 2003). Secondly, it brings diversity in

ideas, perspectives, experiences, and business knowledge to the decision-making process in boardrooms (Baranchuk & Dybvig, 2009). Board diversity can also increase creativity and innovation in boardrooms due to diversity in cognitive abilities, which can also facilitate effective decision-making (Carter, Simkins & Simpson, 2003:36). Thirdly, the resource dependence theory indicates that board diversity helps to link a company to its external environment and secure critical resources, including skills, business contacts, prestige, and legitimacy (Goodstein, Gautum & Boeker, 1994). Fourthly, Rose (2007:405) argues that a higher degree of board diversity may serve as a positive signal to potential job applicants. This will help in the attraction and retention of skills. Finally, corporate boards of qualified individuals of diverse backgrounds and constituencies can help provide a better link with a company's stakeholders, such as consumers and the local community. This can improve a company's reputation and commercial opportunities (Shrader, Blackburn & Iles, 1997).

However, relying on agency and organization theories, opponents contend that board diversity can impact company performance negatively. First, it has been suggested that a more diverse board may not necessarily result in more effective monitoring and decision-making. This is because diverse board members may be appointed as a sign of tokenism, and as such, their contributions may be marginalised (Rose, 2007:406). Secondly, the organisation theory indicates that diversity within the board may significantly constrain its efforts to take decisive action and initiate strategic changes, especially in times of poor company performance and environmental turbulence (Goodstein et al., 1994). Thirdly, diverse board members may bring their individual and constituencies' interests and commitments to the board (Baysinger & Butler, 1985:110), and thus create cabals within the board. The more diverse these interests are, the greater the potential for conflicts and factions to emerge (Baranchuk & Dybvig, 2009:725). This can inhibit boardroom cohesion and performance (Goodstein et al., 1994).

From an agency theory perspective, women often bring fresh perspective on complex issues, and this can help correct informational biases in strategy formulation and problem solving. They have better oversight, display participative leadership which are expected to lead to better performance outcomes. Women's ability to influence board decisions increases with their numbers. From resource dependency theory, female directors bring unique and valuable resources and relationships to their boards (Terjesen, Couto, & Francisco, 2015). Presence of women on the corporate board can help add new resources and improve the efficiency of the firm (Agyemang-Mintah & Schadewitz, 2018).

According to Low et al. (2015) and Adams and Ferreira (2009) cited in Agyemang-Mintah and Schadewitz (2018); gender diversity, improves board monitoring because hiring directors from different backgrounds gives a different lens to the firm where the female members can challenge the status quo. A gender-diverse board is more fruitful in its monitoring roles, as women tend to question management practices and challenge conventional wisdom. Stakeholder theory states that corporations should maximize the welfare of a number of the firm's stakeholders, hence boardroom composition should be adjusted to reflect the expectations of all stakeholders, such as through the appointment of female directors.

According to Daily & Dalton (2003) and Julizaerma and Sori, (2012) cited in Razel (2018), female board directors provide unique perspectives, experiences, and work styles as opposed to their male counterparts, which can greatly enhance deliberations of the board. These attributes will lead to better performance when combined with female characteristics such as communication and listening skills.

My empirical review from the existing literature exhibited inconclusive views in terms of the relationship between board diversity and the banks financial performance. The following are some of the views from the gender diversity perspectives.

Manini and Abdillahi (2015) examined the impact of corporate governance mechanisms on banks' profitability of forty-two sample banks in Kenya for a period of one year. The regression result showed that there was statistically insignificant negative linear relationship between board gender diversity and financial performance.

Stephen, Djan, Bawuah, Halidu, and Kuutol (2015) examined the impact of corporate governance mechanisms on financial performance using 5-year data from 2008-2012 with sample of nine Ghanaian commercial banks. Result revealed that board gender diversity had a significant and negative relationship with return on asset.

Akpan and Amran (2014) examined the relationship between board characteristics and company performance for the period 2010-2012. Results revealed that board gender diversity had a significant and negative effect on performance.

Belhaj and Mateus (2016) investigated the impact of corporate governance on European bank performance during 2002-2011 using sample of 73 banks from 11 European countries. Result

indicated that gender diversity and bank performance were positively and significantly related to bank performance.

Ekadah and Mboya (2011) analysed the effect of board gender diversity on the performance of 44 commercial banks in Kenya covering a 12-year period. Results indicated that board gender diversity shown that a statistically insignificant and negative relationship between board gender diversity and bank performance.

According to the National Bank of Ethiopia Corporate Governance Directive, diversity applies to knowledge, experience, gender and age (Bank Corporate Governance, 2019).

As per the directives, the board may preferably comprise of directors who as a group provide a mixture of core competencies such as banking, finance, accounting, management, economics, legal, business administration, auditing information technology and investment management. The board shall comprise of female directors provided that eligible candidates are available among the shareholders. A director shall be at least 30 years old.

These indicate that National Bank of Ethiopia directives expect board diversity to have a positive impact on the financial performance of the bank. Based on the arguments, the other hypotheses for the study are proposed as follows:

***H2o: There is no statistically significant relationship between board diversity and Bank financial performance (ROA).***

***H2a: There is a statistically significant positive relationship between board diversity and Bank financial performance (ROA).***

### C. Board sub-committees and Bank Financial Performance(ROA)

The separation of corporate ownership and control results in agency conflict problems that require the effective functioning of sub committees as governance mechanisms to solve. The audit committee is seen as an effective sub-committee of a board of directors, which is important in good CG (Abbott, Park & Parker, 2000; Jensen &Meckling, 1976).

According to Dalton et al., (1999) and Spira & Bender (2004) as cited by Johannes (2017), board committees are the critical aspect of monitoring and therefore of the board. This is

because critical processes and decision-making are not done at board level but at committee levels such as the nomination committee, audit and risk committee and remuneration committee. To this end, the establishment of board subcommittees has been strongly recommended as a suitable mechanism for improving corporate governance, by delegating specific tasks from the main board to a smaller group and harnessing the contribution of non-executive directors.

Garcia-Meca and Sanchez- Ballesta (2009) argue that an independent audit committee could enhance the quality and credibility of financial reporting. Cohen and Hanno (2000) emphasize the significance of audit committee independence to appraise management actions regarding risk assessment. In addition, independent directors do not have personal or economic interests in the company in their role of overseeing and monitoring the company's executive management as professional referees (Munro & Buckby, 2008).

Velte (2017) stated that the composition and resourcefulness of audit committee play very important role in ensuring adequate corporate governance quality in the interest of investors and owners of the business.

Empirically, the researcher found that the relationship between board audit committee and bank financial performance in the existing literature is inconclusive. There are two streams of research findings, those that report a positive impact (Abdulazeez, Ndibe and Mercy (2016); Kibrysfaw (2013) and Halidu and Kuutol (2015)) and those that record a negative relationship (Sanyaolu, Adesanmi and Alimi (2018); Bussoli, and Gigante, and Tritto (2015)).

The audit committee is the most important sub-committees that play a crucial role in ensuring the protection of shareholders' interests in matters pertaining to financial reporting and internal control (Mallin, 2010; Klein, 1998).

Below are summarized views of some researchers from my empirical studies in connection with the bank audit committee:

Abdulazeez, Ndibe and Mercy (2016) studied the impact of corporate governance on the performance of Nigerian banks. 15 sample banks for a period of 7 years were part of the study. The regression results showed that the audit committee had positive relationship with performance.

Kibrysfaw (2013) examined the impact of corporate governance mechanism on performance of Ethiopian commercial banks. The study included 9 state and private commercial banks in Ethiopia covering the period 2005-2012. Results reported that availability of audit committee on the board had positive & significant impact on banks performance.

Halidu and Kuutol (2015) examined the extent of board structure, compliance, and its impact on performance. 20 Ghanaian banks were sampled for the period of 2010 and 2013. Results indicated that the number of board committees had a significant and positive impact on return on asset.

Sanyaolu, Adesanmi and Alimi (2018) examined the effect of corporate governance on the financial performance of listed deposit money banks in Nigeria from 2007-2016. The study randomly examined eight (8) deposit money banks listed on the Nigerian stock exchange and obtained data from the annual reports of the banks from 2007-2016. The study found a negative significant relationship between Audit committee and return on asset. The study therefore recommends that companies should embrace and strengthen their audit committee to ensure efficient financial reporting.

Bussoli, Gigante, and Tritto (2015) investigated the impact of corporate governance on bank performance and loan quality. 48 sample banks in Italy for a period of three years were analysed. Results indicated that there was statistically insignificant negative relationship between the number of committees and bank performance.

According to the National Bank of Ethiopia directive, every bank to establish at a minimum audit subcommittee, risk management and compliance sub-committee and human resource affairs sub-committee. The Audit Sub Committee Objective is to provide independent oversight of the bank's financial reporting and internal control system and ensuring checks and balances within the bank. The Risk Management and Compliance Sub-Committee Objective is to oversee senior management's activities in managing credit, market, liquidity, operational, legal and other risk and to ensure that the risk management process is in place and functioning. The Human Resource Affairs Sub-Committee: Primary objective is to provide formal and transparent proposal on the employment and removal of senior management members if they are ineffective, errant or negligent in discharging their responsibilities and on the overall compensation/benefit system of the bank. Each sub-committee shall comprise at least three directors. However, at least one member of the Audit subcommittee should have

accounting or auditing expertise or experience in the field of finance (Bank Corporate Governance, 2019).

This suggests that the National Bank of Ethiopia directive expects that the establishment of board committees may directly or indirectly impact financial company performance positively. Based on the preceding literature, the other hypothesis of this study is proposed as follows:

***H3o: There is no statistically significant relationship between the existence of board committees and Bank financial performance (ROA).***

***H3a: There is a statistically significant positive relationship between the existence of board committees and Bank financial performance (ROA).***

#### **D. Board members' educational qualification and Bank Financial Performance(ROA)**

Boards which are endowed with varied skills can assess the internal business conditions and scan the external environment properly in running the business fruitfully. The possessions of these qualities make them the best suited to driving it forward and achieving the company's goals. In light with this, (Carey, 2008) suggests that the board needs to prepare a description of the role, experience and skills required for a particular new appointment.

Higher education of directors in organizational contexts is positively related to receptivity to innovation, creativity, and better strategic decision-making. Existence of qualified directors' increases banks performance as they promote corporate image and demonstrate accountability and credibility within the management team (Olani & Berhanu, 2015).

Boards are often criticized for failing to meet their governance responsibilities in firms since they lack detailed knowledge and also existence of information asymmetry among the executives and non-executives (Levräu, 2009). These considerations are especially true for bank boards' considering the complexity of the business, the high dynamism and volatility of the markets in recent years and the responsibility of banking boards in supervising and monitoring as a prerequisite for the sound and prudent management of financial intermediaries (OECD, 2005).

A board should consist of directors with diverse business experiences relevant to the firm's existing and future businesses (Madden, 2007). Resource dependency theory focuses on the role that directors play in providing or securing essential resources to an organization. Directors can be classified as support specialists such as lawyers, bankers, insurance company representatives', public relations experts and these specialists provide support in their individual specialized field Hillman, Cannella, and Paetzold (2000) cited in Abdullah and Valentine (2009).

The empirical research finding showed that there is variation in terms of its significance on the overall bank financial performance even though it was noted that it will have positive impact on the Return on asset. Below are the summarized views of some researchers:

Yenesew (2012) investigated the impact of corporate governance mechanisms on firms' financial performance using ten-years data from the year 2010 to 2019 with a sample of eight Ethiopian state and private commercial banks. Results showed that board members educational qualification had a positive and significant effect on return on asset.

Abdurazak (2017) studied effect of corporate governance mechanism on performance of Ethiopian private commercial banks. Panel data covering 11 years 2005-2015 for selected 8 private banks were used. The study reported that directors' educational qualification had positive and result on ROA.

Olani and Berhanu (2015) examined the determinants of the financial performances of commercial banks in Ethiopia from an internal corporate governance practices perspective. Data for the study was collected for a 6-year period for 10 sample banks (2 state owned and 8 private). The analysis showed that the qualification of directors had positive relationship with financial performance of banks.

According to the National Bank of Ethiopia Directives, the board preferably comprise of directors who as a group provide a mixture of core competencies such as banking, finance, accounting, management, economics, legal, business administration, auditing information technology and investment management (Bank Corporate Governance, 2019). The National Bank of Ethiopia directives also explicitly state that at least seventy-five percent of a bank's board members shall hold a minimum of first degree or equivalent from recognized higher learning institution; and the remaining board members, at a minimum, shall complete general

secondary school or its equivalent. (Requirements for persons with significant influence in a bank, 2012)

As per the National Bank of Ethiopia directive, a bank shall give training to directors at least once in a year on priority basis in areas of financial analysis, corporate governance, applicable laws, regulations and directives and risk management and internal control (Bank Corporate Governance, 2019).

This suggests that the National Bank of Ethiopia directive recognizes the educational qualifications of board members as good corporate governance practice. Based on the arguments, the fourth pair of hypotheses for the study is proposed as follows:

***H4o: There is no statistically significant relationship between board members' qualifications and Bank financial performance (ROA).***

***H4a: There is a statistically significant positive relationship between board members' qualification and Bank financial performance (ROA).***

#### **E. Number of Board Meetings & Bank financial performance(ROA)**

According to Andres & Vallelado (2008) as cited by Razel (2017), meetings provide board members with the chance to come together, and to discuss and exchange ideas on how they wish to monitor managers and bank strategy. Hence, the more frequent the meetings, the closer the control over managers, the more relevant the advisory role, factors that lead to a positive impact on performance (proactive boards). By contrast, frequent meetings might also be a result of board reaction to poor performance (reactive boards). Therefore, any hypothesis concerning the influence of board activity on firm performance is an empirical question, possibly yielding either proactive or reactive results (Andres & Vallelado, 2008). Jensen (1993) cited in (Salim et al.2016) takes a contrary view and claims that board meetings might not necessarily be useful because of the shortage in time for directors to exchange meaningful ideas among themselves, the board or the management.

Empirically, the researcher found that the relationship between the number of board meeting and bank financial performance in the existing literature is inconclusive. There are three streams of research findings, those that report a positive impact (Assefa and Megbaru (2014); Firehiwot (2015) and Andres and Vallelado (2008)), those that record a negative relationship

(Malik, Wan, Ahmad, Naseem, & Rehman (2014)) and those that report no association (Salim, Arjomandi, & Seufert (2016)). Below are the findings of the empirical reviews.

Assefa and Megbaru (2014) examined whether corporate governance mechanisms have a significant effect on banks' financial performance and tried to identify the possible determinant factors of corporate governance mechanisms that affect banks' financial performance. Data for 9 banks in Ethiopia (2 state-owned, 7 private) covering a period of 7 years was used for study. The research result showed that the frequency of board meeting had significant and positive association with the return on asset.

Firehiwot (2015) examined the effect of corporate governance in firms' financial performance using ten years data from the year 2005 to 2014 with a sample of nine Ethiopian state and private commercial banks. Results showed that frequency of meeting had a positive and statistically significant influence on return on asset.

Andres and Vallelado (2008) analysed the effectiveness of the boards of directors in monitoring and advising managers in the bank industry. The study was conducted with sample data of 69 banks in 6 OECD countries covering 10-year period. Results indicated that there was positive and insignificant relation between the number of board meetings and bank performance.

Malik, Wan, Ahmad, Naseem, & Rehman (2014) examined 14 sample banks in Pakistan covering a 5-year period. Results indicated that the number of meetings was negatively associated with return on asset. Salim, Arjomandi, & Seufert (2016) studied the effect of corporate governance on Australian banks' performance for the period 1999-2013. The result reported that the number of board meetings has no significant effect on the ratio on return on asset.

According to the National Bank of Ethiopia directive the board shall set up and put in use rules for the manner of conducting board meetings and board meetings shall be held at least once in a month on the date, at the venue fixed in accordance with the rules for manner of conducting board meetings, the board of director shall attend in person at least 75% of the board meetings of a bank within the financial year. Failure to do so, unless adequately justified and accepted by shareholders general meeting, will render automatic cancellation of his/her seat on the board. (Bank Corporate Governance, 2019).

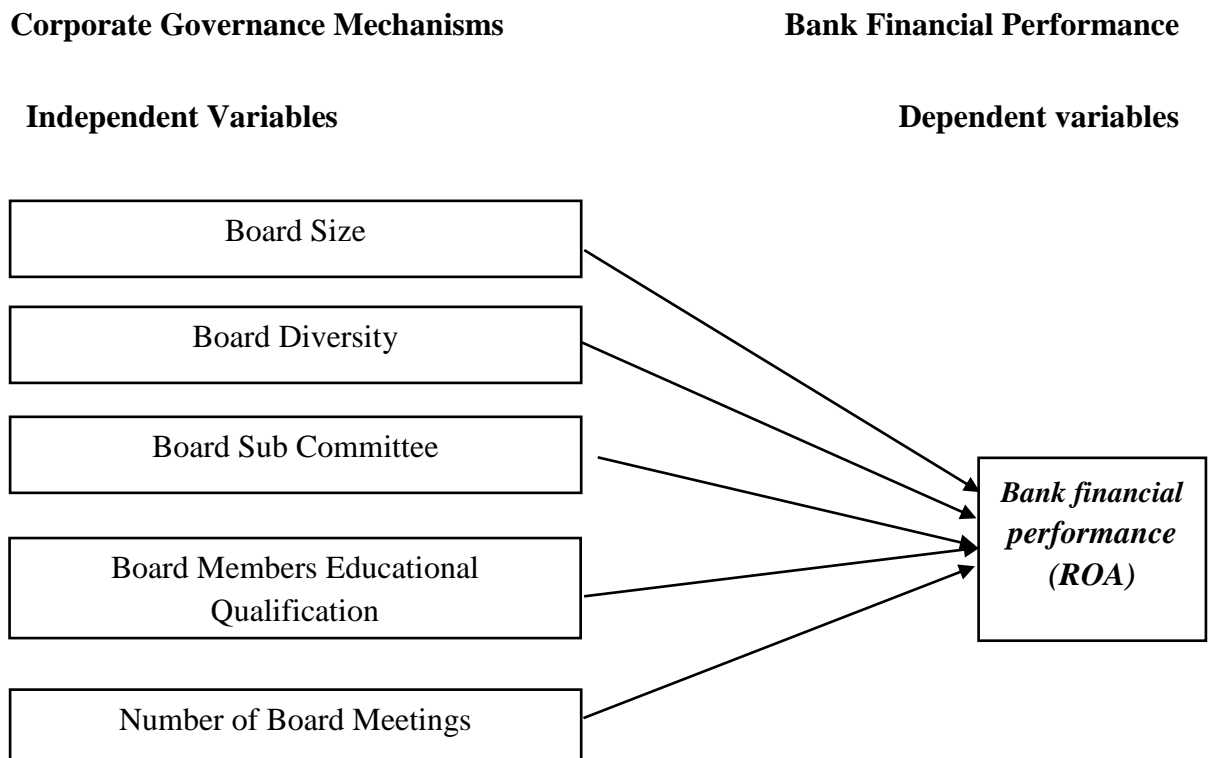
This implies that National Bank of Ethiopia directive expects a higher frequency of board meetings to impact positively on financial performance. Based on the arguments, the fifth pair of hypotheses for the study will be:

*H5o: There is no statistically significant relationship between board meeting and Bank financial performance (ROA).*

*H5a: There is a statistically significant positive relationship between board meeting and Bank financial performance (ROA).*

#### 2.4. Conceptual framework

The main objective of this study is to show the impact of Corporate Governance on Performance of banks in the case of Zemen Bank Share Company. The below conceptual framework is developed after review of literature discussed in the previous chapter. The study is based on the presumption that Corporate governance factors that are used in this study are Board Size, Board diversity, Board sub-committees, Board members’ educational qualification and number of Board Meetings as independent variables and Return on Asset (ROA) is taken as dependent variables to measure bank performance.



**Figure 2.1: Conceptual Framework**

## **CHAPTER THREE**

### **RESEARCH METHODOLOGY**

#### **3.1. Introduction**

This chapter focuses on the research methodology used in the study and how it relates to the research objectives. It presents the research methodology. The main aim of this study is to explore and understand how corporate governance affects company performance. This chapter has sub-sections presenting the research design, population and sampling technique used, study variables and their measurements, data sources and collection methods, data analysis method and model specification.

#### **3.2. Research Design**

The main aim of this study is to assess the corporate governance practices and impact on the financial performances of Zemen Bank Share Company. In doing so, the research will explore, describe, and critically examine the bank corporate governance practices according to the international and best corporate practices. It also specifically reviews the bank corporate governance practices in line with the National Bank of Ethiopia directives and ultimately their impacts on the bank performances.

As per the research questions and objectives, descriptive and inferential analyses have been applied for this study. The research describing the corporate governance practices of the Zemen Bank Share Company. The research objective is to assess the effect of corporate governance on bank performance; hence both descriptive and inferential analyses have been used to test the hypothesis of causal relationship between the dependent and independent variables.

The researcher considers a descriptive study because it will depict corporate governance practices and gives meanings and draws conclusion from the data that are described. The descriptive statistics summarize the characteristics of a data set. It assesses corporate governance practices considering standards, NBE directives, shareholders, boards, and stakeholders' views.

The study considers inferential studies that involve regression analysis to test the nature of relationships between a dependent variable and independent variables. The study applies the quantitative research that is expressed in numbers and graphs. It is used to test assumptions. This is used to establish facts about a topic. It includes observations recorded as numbers and surveys questions.

The research also applies qualitative research to understand concepts, thoughts or experiences. These qualitative methods include questionnaire, interview questions, observations described in words, and literature reviews that explore concepts and theories.

### **3.3. Data Sources and Collection Technique**

Data were collected both from the primary and secondary sources. The study took the advantage of both primary (Questionnaire and Interview) and secondary data sources.

In this study, the potential respondents are boards of directors, CEOs, and Directors. These are high profile, busy and hardly accessible people with a tight time schedule. Most of the information will be obtained from the bank's senior management and board of directors located at their head offices.

A letter from the Addis Ababa University, Graduate program Coordination office that requested support to conduct the research is issued to the bank. The Letter addressed the bank Chief Executive Office, seeking permission to run a research via a paper-based survey questionnaire & interview, and to get access for secondary documents.

Primary and secondary data sources have been used to collect the quantitative data of the study. Banks' annual reports for the ten-year period covering 2011- 2019 have been used as secondary data to obtain inputs used for the calculation of the figures for dependent variables of Return on Asset (ROA) and for control variables of bank size and age.

For this study, descriptive research design is adopted that include questionnaires, observation method and interviews. The questionnaires and interview results are triangulated to come up with the best research findings. Primary data is obtained by distributing questionnaires to the top management, employees and also to the board of directors during the monthly board meeting.

Data for board size and board subcommittee have also been obtained from the annual reports. Questionnaires distributed to board members and managers have been sources of primary data. Variables of board diversity, number of board meetings and board members educational qualifications have been collected from primary sources.

Other secondary sources used for this research are Articles, Books, Websites of the banks, Magazine journals, and Annual reports relates to the Banking Sectors and the annual reports disclosed by the National Banks of Ethiopia (NBE).

In addition to the above, the search engines such as Google, Yahoo, and Bing were effective for a wider range of information from various groups of research specialists in contributing and sharing their knowledge relating to the topic. Besides that, e-journals were found to serve as references to the study.

### **3.4. Population and Targeted Group: Census Method**

Zemen Bank has a structure Board with the ultimate responsibility for the overall activities of the Bank. The bank has developed its own Code of Corporate Governance and adopted eight Charters applicable for the bank as Code of Corporate Governance.

As the research focuses on the Corporate governance practices of the bank and its impact on the bank financial performance (ROA), most of the information obtained from the bank's board of directors, board secretary and board subcommittee members located at the bank head offices.

The bank board room is comprised of Nine (9) Board Directors and one (1) Board Secretary. The board has also established Seven (7) different board Sub committees. The bank board sub-committees are - Audit Sub-Committee, Human Resource Affairs Sub-Committee, Loan Review Committee, Board Risk and Compliance Sub-Committee, Strategy and Budget Sub-Committee, Information Technology Sub-Committee, and The Headquarters Building Construction Committee. Each board Sub-Committee comprise of Three (3) directors each. The total numbers of sub-committee members are twenty-one.

For this study, the total population and target groups are all board room directors, board secretary and Board subcommittee members. Data collected from the Zemen bank board members, Board secretary and board subcommittee groups with Census method. Hence the

total number of the target group are Thirty-One (31) which include Nine Board Directors, One Board Secretary and Twenty-One members of the board Sub-Committee.

Primary data obtained by distributing questionnaires to the board directors, board secretary, board sub-committee and top management. Questionnaires for board of directors collected during the monthly board meeting. The questionnaires and interview results triangulated to come up with the best research findings.

In measuring the performances, in accounting terms, secondary data obtained from the bank annual reports are considered. The study used structured review of documents, and Zemen bank financial data for ten years were collected covering a period 2011 to 2019. The researcher also examines the bank's annual reports, Charter of Boards of Directors and Sub Committees.

### **3.5. Data Analysis Method**

The data collected from primary and secondary sources analyzed using appropriate statistical tools. The researcher conducts the combination of descriptive and evaluation research to provide further insight into the research problem and measure the performance of the corporate governance.

The study employs descriptive data analysis to describe the phenomena of the variables using minimum, maximum, mean and standard deviation. Correlation analysis using Pearson correlation is used to determine the association between the variables. Correlation analysis measures the strength of the linear relationship between variables while regression analysis provides a "best-fit" mathematical equation for the values of the variables used in determining and interpreting linear relationships of variables (Weiers, 2008). Hence, multiple linear regression model has been used to conduct inferential analysis to determine causal relation of the panel data. The research considers multiple regression model to examine the relationship between the Corporate Governance variables and their relationship with bank performance. This method will analyze the relationship by using dependent variables and independent variables to test the hypotheses.

The study considered major inferential analysis approach including multiple regression together with correlation analysis to predict the value of the variable based on the value of two

or more other variables. These analysis approaches are used to examine the relationship between dependent and independent variables.

The SPSS is used to assess and analyze the collected data to examine the relationship between corporate governance practices and Zemen Bank Share company financial performance. Descriptive techniques such as means, standard deviation (Std.) and coefficient of variation (CV) were used to describe the variables. Finally based on panel data regression analysis a suitable conclusion is drawn and some managerial implications are suggested.

### **3.6. Variables and Measurement Model Specification**

This research analyzes the dependent, independent, and control variables used in the econometric analysis. Dependent variable is the ROA, return on asset, is net income divided by total assets.

The independent corporate governance variables include Board Size, Board diversity, Board sub-committees, Board members' educational qualification and number of Board Meetings.

The Control Variables considered are the bank characteristics that can affect both a bank's performance and its corporate governance practices, in different ways. The two control variables are the bank size and age.

Following review of theoretical and empirical literature, below are the selected variables used as proxies to study the effect of corporate governance on the bank performance.

#### **3.6.1. Dependent Variable: Performance**

**Performance was proxy with Return on asset (ROA).** This is measured as ROA (Return on Asset): It is the variable used to measure bank performance. The ratio reflects the ability of a bank's management to generate profits from assets. It would be measured as:

$$\text{Return on Asset (RoA)} = \frac{\text{Profit before tax}}{\text{Total assets}} \times 100\%$$

### **3.6.2. Independent Variable: Corporate Governance**

- **Board Size**

It is a measure of the total number of directors serving as board of director.

- **Board Gender Diversity**

The ratio of age, gender, ethnicity, religion, work career and life experiences of the board directors to total board members.

- **Number of Board Committees**

It is measured as the count of the total number of board sub-committees within the bank.

- **Board members' educational qualification**

It is measured as the proportion of board members having academic qualifications in either of the fields of finance, accounting, economics, banking, auditing, business administration, law, information technology, investment management to total members.

- **Number of Board Meetings**

The count of total board committee and full board meetings held in a year.

### **3.6.3. Control Variables**

- **Bank Size & Age**

It is measured by the natural logarithm of total assets at year-end.

### **Summary of the research hypotheses**

Statistical procedures are typically used to test the relationship between two or more variables. Statistical validity addresses the question of whether the statistical conclusions drawn from the results of a study are reasonable. The concepts of hypothesis testing and statistical evaluation are interrelated, and they provide the foundation for evaluating statistical validity (Marczyk, Dematteo & Festinger, 2005).

The below table shows all the hypotheses for the study. Column 2 presents the tested relationship based on empirical evidence and Column 3 reports the predicted sign based on empirical findings.

**Table 3.1: Summary of the five research hypotheses**

Hypotheses	Tested relationships	Predicted sign
H1	Board Size and Bank Financial Performance(ROA)	+
H2	Board Gender Diversity and Bank Financial Performance (ROA)	+
H3	Board Sub-committees and Bank Financial Performance(ROA)	+
H4	Board Members Educational Qualification & Bank Financial Performance(ROA)	+
H5	Number of Board Meetings & Bank Financial Performance(ROA)	+

### 3.7. Model specification

There are a number of factors that may affect corporate governance and a bank’s financial performance. The factors to be used for analysis in this study include Board Size, Board diversity, Board sub-committees, Board members educational qualification and number of Board Meetings. Ordinary least square method using panel data would be made used of in the analysis. This study, however, is confined to the relationship of five factors that are variables which are briefly described above.

To test the study, a panel data model is used. A panel of data embodies information across both time and space (Brooks, 2014). The data for this study comprises of both time series and cross-sectional elements as it considers Zemen bank over a period of 5 years.

To estimate the effect of corporate governance on banks’ financial performance, the following general empirical research model is used. The panel data regression model was selected based on review of literature.

$$Y_{i,t} = \alpha + \sum \beta K X_{it} + \varepsilon_{it}$$

Where.

- ✓  $Y_{i,t}$  represents the dependent variable, representing the financial performance of the bank  $i$  for time  $t$
- ✓  $\alpha$  is the intercept
- ✓  $\beta K$  represents the vector of parameters to be estimated on the explanatory variables
- ✓  $X_{it}$  represents the explanatory variable of the sample banks  $i$  for time  $t$
- ✓  $\varepsilon_{it}$  represents the error term

The model used for this study was adapted from Enilolobo et al (2019) where it was written as:

$$PER = f(ACM, BND, BSZ, SEC, OWN) \dots\dots\dots(1)$$

With relation to this work, the model in equation (1) was modified as follows.

$$ROA = f(BSZ, BGD, BSCM, BEQ, BMT) \dots\dots\dots(2)$$

Where:

ROA = Return on assets (ROA), proxy by Performance

BSZ = Board Size, proxy by actual number of directors on the board

BGD=Board gender diversity, proxy by ratio of board directors diversity to total board members

BSCM = Board Sub-Committee, proxy by actual number board sub-committees within the bank

BEQ = Board's members' educational qualification, proxy by the proportion of board members having academic qualifications

BMT = Board meeting, proxy by actual number of total board committee and full board meetings held in a year

This can be expressed using linear equation as.

$$ROA_{i,t} = \alpha + \beta_1 BSZ_{i,t} + \beta_2 BGD_{i,t} + \beta_3 BSCM_{i,t} + \beta_4 BEQ_{i,t} + \beta_5 BMT_{i,t} + \mu$$

Where.

$ROA_{i,t}$  represents measure of bank performance of the bank  $i$  for time  $t$

$BS_{i,t}$  represents board size of the bank  $i$  for time  $t$

$BD_{i,t}$  represents board diversity of the bank  $i$  for time  $t$

$BSC_{i,t}$  represents board Sub-Committee of the bank  $i$  for time  $t$

$BME_{i,t}$  represents Board's members educational qualification of the bank  $i$  for time  $t$

$BM_{i,t}$  represents Board meeting of the bank  $i$  for time  $t$

$\mu$  represents random error term or Stochastic

### **3.8. Pilot testing of the instrument**

A pilot test was conducted to field test the reliability and the validity of the data to be collected using the questionnaire. The questionnaire was tested to a selected sample which was similar to the actual sample. Subjects in the actual sample was not be used in this pilot study. Same procedures to be used in the actual data collection exercise were used for the pretesting exercise. The pretest sample was 10% of the sample size.

#### **3.8.1. Validity of instruments**

According to Kothari (2004) validity is the degree by which the sample of the test items represents the content the test is designed to measure. The study questionnaire was scrutinized for content validity by experts in business research. Factor analysis was employed to test the suitability of the research instrument. The suggestions on the content and structure were included to improve the final draft of the instrument.

### 3.8.2. Reliability Analysis

Reliability of the questionnaire was evaluated through Cronbach's Alpha which measures the internal consistency. Cronbach's alpha was calculated by application of SPSS for reliability analysis. The value of the alpha coefficient ranges from 0-1 and may be used to describe the reliability of factors extracted from dichotomous and or multi-point formatted questionnaires or scales. A higher value shows a more reliable generated scale. Cooper & Schindler (2008) has indicated 0.7 to be an acceptable reliability coefficient. Table 3.2 shows that Cronbach's Alpha 0.879. This illustrates that the questionnaire was reliable as the reliability value exceeded the prescribed threshold of 0.7.

**Table 3.2: Overall questionnaire test**

<b>Reliability Statistics</b>		
Cronbach's Alpha	Cronbach's Alpha Based on Standardized Items	N of Items
.820	.879	55

## CHAPTER FOUR

### DATA ANALYSIS AND DISCUSSION

#### 4.1. Introduction

This chapter of the study analyses the data collected based on the research question set out for the study. The first research question was to ascertain how the internal corporate governance mechanisms of the bank board room structured and function including board size, board diversity, Board sub-committees, Board members educational qualifications and number of board meetings. The second research question was to investigate how the bank board room functioning and monitoring the financial performance of the bank by using financial ratio including Return on Asset (ROA).

#### 4.2. Response rate

**Table 4.1. Respondents' response rate**

Questionnaires Distributed	Questionnaires Returned	Percentage
31	31	100

To determine the actual number of responses who actively participated in the study, analysis of the response rate was conducted as shown in the table 4.1 above. The data collection instrument, questionnaires, were distributed to 31 board directors and out of the 31 questionnaires, all the questionnaires were received back. All were fully completed and that makes a response rate of 100%.

### 4.3. Descriptive analysis

**Table 4.2. Socio-Demographic Information of the respondents**

<b>Gender</b>					
		Frequency	Percent	Valid Percent	Cumulative Percent
	Male	28	90.3	90.3	90.3
	Female	3	9.7	9.7	100.0
	Total	31	100.0	100.0	
<b>Age</b>					
	30-39 Year	1	3.2	3.2	3.2
	40-49 Year	17	54.8	54.8	58.1
	50-59 Year	8	25.8	25.8	83.9
	60 and Above Year	5	16.1	16.1	100.0
	Total	31	100.0	100.0	
<b>Work experience</b>					
	1-5 Years	1	3.2	3.2	3.2
	6-10 Years	4	12.9	12.9	16.1
	11-15 Years	10	32.3	32.3	48.4
	16-20 Years	11	35.5	35.5	83.9
	Above 20 Years	5	16.1	16.1	100.0
	Total	31	100.0	100.0	
<b>Highest level of education</b>					
	MA/MSc	29	93.5	93.5	93.5
	PhD and above	2	6.5	6.5	100.0
	Total	31	100.0	100.0	

Source: Own survey, 2020

As shown in table 4.2 above, concerning gender distribution of respondents, 28 (90.3%) were male whereas 3 (9.7%) females. This shows that the gender distribution of the respondents is male dominated. As shown in the table 4.2 above, regard to the age structure 1

(3.2%) of respondents were the age group of 30-39 years, 17 (54.8%) of respondents were between the age group of 40-49 years, 8 (25.8%) of respondents were aged 50-59 years and the rest 5 (16.1%) were above 60 years. This implies that the Bank is relatively occupied by senior professional. As shown in the same above, concerning work experience distribution of respondents, 1 (3.2%) were in a range of 1-5 years, 4 (12.9%) were in a range of 6-10 years, 10 (32.3%) were above 11-15 years, 11 (35.5%) were in a range of 16-20 year and 5 (16.1%) were above 20 years. This shows that the bank is represented by senior staffs. The above table also shows the academic qualification of the respondents. As indicated in the table, 29 (93.5%) of the total respondents are of second-degree holder followed by PhD and above degree holders 2 (6.5%). This implies that the Bank board has well educated directors.

**Table 4.3: Board size**

Board size	SD	D	N	A	SA	Mean	Sd.
The existing board size is the idea and perfect size recommended for any bank board. The size is in accordance with the National Bank of Ethiopia directive within the range of maximum and minimum number of board members.	0.0%	0.0%	0.0%	35.5%	64.5%	4.65	.486
The existing board has sufficient size and composition to perform its role and responsibilities without due disruption.	0.0%	0.0%	0.0%	38.7%	61.3% %	4.61	.495
As a member of the board, you feel that the existing bank board has too many directors that make the board unproductive with ineffective communication and delayed the board decision making process.	54.8	35.5%	9.7%	0.0%	0.0%	1.55	.675
The bank board capacity for monitoring increases as more directors are added, and the increased board members number benefit outweighed the incremental cost of poorer communication and decision-making interruption.	41.9%	29.0%	9.7%	16.1%	3.2%	2.10	1.221

As one of the board of directors, you believe that the bank board size should be small to promote critical, genuine, and intellectual deliberation and involvement among members, which presumably lead to effective corporate decision- making, monitoring and	25.8%	29.0%	12.9%	22.6%	9.7%	2.61	1.358
The board has sufficient size so that, there are sufficient board members to discharge the board’s workload.	0.0%	0.0%	0.0%	45.2%	54.8%	4.55	.506
As director you believe that the existing board size is not large enough and the board room is benefiting the advantage of larger boards to get diversified expert advice and opinions around the table compared to a small board.	19.4%	6.5%	6.5%	38.7%	29.0%	3.52	1.480
The board size is not large enough and expected to increase board diversity in relation to experience, skills, gender and the bank financial performance (ROA).	0.0%	0.0%	19.4%	41.9%	38.7%	4.19	.749
Bank has established recommendable board size with board members that have adequate skills and competencies to carry out their responsibilities.	0.0%	0.0%	3.2%	51.6%	45.2%	4.42	.564
The numbers of board members are not too many members; hence board members discussions are not constrained, and all board members are meaningfully engaged in and contribute to deliberations.	0.0%	0.0%	0.0%	45.2%	54.8%	4.55	.506
The board size has helped the board members to establish ease of interpersonal relations at the board table.	0.0%	0.0%	9.7%	45.2%	45.2%	4.35	.661
The board members and its size are manageable. Directors do not face challenge to know their fellow board members and, to gain trust & confidence in them.	0.0%	0.0%	6.5%	35.5%	58.1%	4.52	.626
As a member of the board room, you believe that increasing the existing board size has a positive and significant impact on the bank Financial Performance(ROA).	25.8%	19.4%	0.0%	29.0%	25.8%	3.10	1.620

Source: Own survey, 2020

As shown in the table 4.3 above, the questionnaire rated by the respondents considering the rating scale, strongly agree (SA), Agree (A), Neutral (N), Disagree(D) and Strongly Disagree (SD).

Most of the respondents rated the existing board size as ideal. The size is in accordance with the National Bank of Ethiopia directive. Most of the respondents rated the existing board as sufficient size and composition to perform its role and responsibilities without due disruption as shown by mean 4.61.

Most directors strongly disagree at 54.8 % for the questionnaire that questioned them if they feel that the existing bank board has too many directors that make the board unproductive with ineffective communication and delayed the board decision making process. They were also responded with strong disagreement for the assessment if they think that the board capacity for monitoring increases as more directors are added, and the increased board members number benefit outweighed the incremental cost of poorer communication and decision- making interruption.

Many directors at 29% disagree and do not believe the idea that the bank board size should be small to promote critical, genuine and intellectual deliberation and involvement among members, which presumably lead to effective corporate decision- making, monitoring.

Most of the respondents rated agree and confirmed that the board has sufficient size so that, there are sufficient board members to discharge the board's workload as shown by 54.8%. The directors are also believed that the existing board size is not large enough and the board room is benefiting the advantage of larger boards to get diversified expert advice and opinions around the table compared to a small board. The board of directors are also believed that the board size is not large enough and expected to increase board diversity in relation to experience, skills, gender and the bank financial performance (ROA) as shown by majority of at 41.9%.

The majority of board directors responded that the bank has established recommendable board size with board members that have adequate skills and competencies to carry out their responsibilities. They also strongly agreed that the numbers of board members are not too many members; hence board members' discussions are not constrained, and all board members are meaningfully engaged in and contribute to deliberations. Most of the directors

are strongly agreed and responded that the board size has helped the board members to establish ease of interpersonal relations at the board table, to gain trust & confidence in them.

Most of the respondents as a member of the board room rated agree and believed that increasing the existing board size has a positive and significant impact on the bank financial performance (ROA).

**Table 4.4: Board Diversity**

Board diversity	SD	D	N	A	SA	Mean	Sd.
The bank board has a diversified and well-balanced board of directors with as various attributes, such as age, gender, ethnicity, culture, religion, career and life experiences.	0.0%	12.9%	3.2%	48.4%	35.5%	4.06	.964
The diversity in the boardroom increases board independence and improves executive monitoring.	0.0%	0.0%	0.0%	32.3%	67.7%	4.68	.475
The board members diversity brings diversity in ideas, perspectives, experiences and business knowledge to the decision-making process in boardrooms.	0.0%	0.0%	6.5%	35.5%	58.1%	4.52	.626
The board diversity also increased creativity and innovation in boardrooms due to diversity in reasoning abilities, which can also facilitate effective decision-making.	0.0%	0.0%	12.9%	38.7%	48.4%	4.35	.709
As a director and members of the board room, you believe that diversity as a positive force, the existence of multiple and divergent viewpoints within a board significantly enhance the bank financial performance (ROA).	0.0%	0.0%	6.5%	35.5%	58.1%	4.52	.626
The board room is gender diversified and has Women directors who have better oversight, and their influence to the board decisions increases with their numbers.	0.0%	0.0%	35.5%	25.8%	38.7%	4.03	.875
The diversity of the board directors helps to improve the bank and its financial performance as it links the bank to its external environment and secure critical resources, including skills, business contacts, reputation & business opportunities.	0.0%	0.0%	19.4%	54.8%	25.8%	4.06	.680

The diversity of the bank board has negative impact on the effective monitoring and decision-making of the board room.	48.4%	19.4%	3.2%	19.4%	9.7%	2.23	1.477
The more diverse board members bring their individual interests and commitments to the board that inhibit boardroom cohesion and impacted the overall financial performance of the bank.	25.8%	22.6%	6.5%	29.0%	16.1%	2.87	1.500

Source: Own survey, 2020

As shown in the table 4.4 above, most of the board directors rated to agree at 48.4% that the bank board has a diversified and well-balanced board of directors with as various attributes, such as age, gender, ethnicity, culture, religion, career and life experiences. The majority of directors are also strongly agreed that diversity in the boardroom increases board independence and improves executive monitoring as shown by 67.7%. Most of the board members strongly believed that the diversity brings diversity in ideas, perspectives, experiences, and business knowledge to the decision-making process in boardrooms.

The directors also strongly agreed that the board diversity increased creativity and innovation in boardrooms due to diversity in reasoning abilities, which also facilitate effective decision-making. As a director and members of the board room, 58.1% of the directors strongly believed diversity as a positive force, the existence of multiple and a divergent viewpoint within a board significantly enhances the bank financial performance (ROA). They also believed that the board room is gender diversified and has Women directors who have better oversight, and their influence to the board decisions increases with their numbers.

Most of the directors at 54.8 % rated that the diversity of the board directors helped to improve the bank and its financial performance as it links the bank to its external environment and secure critical resources, including skills, business contacts, reputation & business opportunities. They also strongly disagreed for the opinion that the diversity of the bank board has negative impact on the effective monitoring and decision-making of the board room. Rather, the board of directors believed that the more diverse board members bring their individual commitments to the board that improved the boardroom solidity and impacted the overall financial performance of the bank.

**Table 4.5: Board Sub Committees**

	SD	D	N	A	SA	Mean	Sd.
<b>Board Sub Committees</b>							
The bank board room has established audit subcommittee, risk management and compliance sub-committee and human resource affairs sub-committee.	0.0%	0.0%	6.5%	16.1%	77.4%	4.71	.588
The establishment of board subcommittees has played significant role and improved the bank corporate governance as the main board delegate specific tasks to the board subcommittee and utilizing the contribution of non-executive directors.	0.0%	0.0%	6.5%	25.8%	67.7%	4.61	.615
The Audit Sub-Committee provides independent oversight of the bank's financial reporting and internal control system and ensure checks and balances within the bank.	0.0%	0.0%	6.5%	19.4%	74.2%	4.68	.599
The Risk Management and Compliance Sub-Committee oversees senior management's activities in managing credit, market, liquidity, operational, legal and other risk and ensure that the risk management process is in place and functioning.	0.0%	0.0%	0.0%	29.0%	71.0%	4.71	.461
The Human Resource Affairs Sub-Committee provides formal and transparent proposal on the employment and removal of senior management members if they are ineffective, errant or negligent in discharging their responsibilities and on the overall compensation	0.0%	0.0%	6.5%	22.6%	71.0%	4.65	.608
As one of the board of directors, you believe that the effectiveness of the board is influenced by board committees as the regulatory recommendations and the complexity of bank activities place emphasis on the importance of board committees.	0.0%	0.0%	6.5%	32.3%	61.3%	4.55	.624
The bank board uses the above-board sub-committee structures to facilitate, evaluate, and ratify long-term investment decisions and to monitor the performance of senior management.	0.0%	0.0%	0.0%	41.9%	58.1%	4.58	.502
As one of the board of directors, you believe that the different board sub-committees of the existing board room has a positive and significant impact on the bank Financial Performance (ROA).	0.0%	0.0%	0.0%	22.6%	77.4%	4.77	.425

Source: Own survey, 2020

As shown in the table 4.5 above, the directors confirmed that the bank board room has established audit subcommittee, risk management and compliance sub-committee and human resource affairs sub-committee.

Most board directors strongly agreed at 67.7% of the query that the establishment of board subcommittees has played significant role and improved the bank corporate governance as the main board delegate specific tasks to the board subcommittee and utilizing the contribution of non-executive directors. 74.2% of the directors strongly believed that the Audit Sub-Committee provides independent oversight of the bank's financial reporting and internal control system and ensure checks and balances within the bank.

The directors strongly agreed that the Risk Management and Compliance Sub-Committee oversees senior management's activities in managing credit, market, liquidity, operational, legal and other risk and ensure that the risk management process is in place and functioning. 71% of the directors are also strongly believed that the Human Resource Affairs Sub-Committee provides formal and transparent proposal on the employment and removal of senior management members and on the overall compensation.

The board of directors strongly believed and confirmed that the effectiveness of the board is influenced by board committees as the regulatory recommendations and the complexity of bank activities place emphasis on the importance of board committees. They also strongly commented that the bank board uses the above-board sub- committee structures to facilitate, evaluate, and ratify long-term investment decisions and to monitor the performance of senior management. Most of the board members also strongly confirmed that these different board sub-committees of the existing board room have a positive and significant impact on the bank Financial Performance (ROA).

**Table 4.6: Board Members Education**

	SD	D	N	A	SA	Mean	Sd.
Board Members education							
The bank board comprise of directors who as a group provide a mixture of core competencies such as banking, finance, accounting, management, economics, legal, business administration, auditing information technology and investment management.	0.0%	0.0%	6.5%	16.1%	77.4%	4.71	.588
The bank board room has directors with higher educational qualifications and contributed for the board room to be innovative, creative, and better in strategic decision-making.	0.0%	0.0%	0.0%	35.5%	64.5%	4.65	.486
The existence of qualified directors in the bank board room has increased the bank performance as they promote corporate image and demonstrate accountability and credibility within the team.	0.0%	0.0%	6.5%	32.3%	61.3%	4.55	.624
The bank board room plays an important role in formulating and implementing business strategy as it is composed of directors who bringing expertise and knowledge.	0.0%	0.0%	6.5%	32.3%	61.3%	4.55	.624
As one of the board directors, you emphasize on the board of directors' qualification rather experience for the bank existing and future business success.	0.0%	19.4%	25.8%	38.7%	16.1%	3.52	.996
The bank board has directors with varied skills that can assess the internal business conditions and scan the external environment properly in running the bank business successfully.	0.0%	3.2%	0.0%	61.3%	35.5%	4.29	.643
As one of the bank board, you believe that the educational qualification of the existing board room has a positive and significant impact on the bank Financial Performance (ROA).	0.0%	6.5%	16.1%	25.8%	51.6%	4.23	.956

Source: Own survey, 2020

As shown in the table 4.6 above, most of the respondents strongly agreed that the bank board comprise of directors who as a group provide a mixture of core competencies such as banking, finance, accounting, management, economics, legal, business administration, auditing information technology and investment management. 64.5% of the board directors

strongly agreed that the bank board room has directors with higher educational qualifications and contributed for the board room to be innovative, creative, and better in strategic decision-making.

Most of the directors responded that the existence of qualified directors in the bank board room has increased the bank performance as they promoted corporate image and demonstrate accountability and credibility within the team. 61.3 % of the board of directors strongly agreed that the bank board room plays an important role in formulating and implementing business strategy as it is composed of directors who bringing expertise and knowledge.

Most of the respondents agreed and emphasized on the board of directors' qualification rather experience for the bank existing and future business success. The board of directors agreed that the bank board has directors with varied skills that can assess the internal business conditions and scan the external environment properly in running the bank business successfully. 51.6 % of the directors strongly agreed and believed that the educational qualification of the existing board room has a positive and significant impact on the bank Financial Performance (ROA).

**Table 4.7: Number of board meetings**

<b>Number of board meetings</b>	<b>SD</b>	<b>D</b>	<b>N</b>	<b>A</b>	<b>SA</b>	<b>Mean</b>	<b>Sd.</b>
The intensity of board activity is measured by the frequency of board meetings as it indicates an active monitoring role of the board.	0.0%	0.0%	0.0%	51.6%	48.4%	4.48	.508
The bank board meetings provide useful information in a timely manner which is critical for the board's effectiveness.	0.0%	0.0%	6.5%	38.7%	54.8%	4.48	.626
Board meeting time is adequate and has significant contribution for improving the effectiveness of the bank board.	0.0%	0.0%	0.0%	32.3%	67.7%	4.68	.475
The more frequent of the bank board meetings provide board members with the chance to come together, and to discuss and exchange ideas on how they wish to monitor managers and bank strategy.	0.0%	0.0%	12.9%	54.8%	32.3%	4.19	.654

The bank board members are meeting more frequently beyond their regular schedule meeting and it has contributed more to improve board performance and tends to generate higher for the bank financial performance (ROA).	0.0%	6.5%	25.8%	25.8%	41.9%	4.03	.983
The boards of directors believe that increasing the level of board activity through board meetings lead to better bank achievement and financial performance.	0.0%	0.0%	9.7%	54.8%	35.5%	4.26	.631
As one of the board directors, you believe that frequent board meetings is not necessarily and useful because of the shortage in time for directors to exchange meaningful ideas among themselves.	9.7%	48.4%	3.2%	16.1%	22.6%	2.94	1.413
Member of the bank board well aware and know that a director should attend in person at least 75% of the board meetings of a bank within the financial year.	0.0%	0.0%	6.5%	48.4%	45.2%	4.39	.615
The current practice of the board meetings is to 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 board meetings.	0.0%	0.0%	19.4%	35.5%	45.2%	4.26	.773
The board member has showed their interest and brought their concern to the board table to increase the number of board meeting as it will have significant contribution for the bank financial performance (ROA).	0.0%	0.0%	35.5%	29.0%	35.5%	4.00	.856
As one of the bank board directors, you believe that the frequent (increased) board meeting has a positive and significant impact on the bank Financial Performance (ROA).	0.0%	0.0%	38.7%	35.5%	25.8%	3.87	.806

Source: Own survey, 2020

As shown in the table 4.7 above, most of the board directors agreed that the intensity of board activity is measured by the frequency of board meetings as it indicates an active monitoring role of the board. The board of directors strongly agreed that the bank board meetings provide useful information in a timely manner which is critical for the board's effectiveness. 67.7% of

the board of director strongly agreed that the board meeting time is adequate and has significant contribution for improving the effectiveness of the bank board.

The majority of board members agreed that the more frequent of the bank board meetings provide board members with the chance to come together, and to discuss and exchange ideas on how they wish to monitor managers and bank strategy. Most of the board of directors agreed that the bank board members are meeting more frequently beyond their regular schedule meeting and it has contributed more to improve board performance and tends to generate higher for the bank financial performance (ROA). 54.8% of the board of directors believed that increasing the level of board activity through board meetings lead to better bank achievement and financial performance.

Most of the directors ,48.4% of the directors believed that frequent board meetings are necessarily and useful as the more frequent meeting will help for directors to exchange meaningful ideas among themselves. The majority of the directors are also agreed that member of the bank board aware and know that a director should attend in person at least 75% of the board meetings of a bank within the financial year. It is also confirmed that the current practice of the board meetings is to hold at least once in a month on the date and at the venue fixed in accordance with the rules for manner of conducting board meetings.

The majority of the board member have showed their interest and brought their concern to the board table to increase the number of board meeting as it will have significant contribution for the bank financial performance (ROA). 38.7% of the board of directors kept neural to confirm or in dilemma to believe the frequent (increased) board meeting has a positive and significant impact on the bank Financial Performance (ROA).

**Table 4.8: Return on Asset**

Return on Asset	SD	D	N	A	SA	Mean	Sd.
The bank had good improvement in its financial performance and the return on Assets has been improved during the last 5 years.	0.0%	0.0%	6.5%	38.7%	54.8%	4.48	.626
The Corporate Governance practices of the bank board during the last five years has been improving and has significant contribution for the overall bank achievement and financial performance success specifically on Return on Asset (ROA).	0.0%	6.5%	9.7%	38.7%	45.2%	4.23	.884
As a member of the board room, you believe that the Internal Corporate Governance mechanism of the existing board specifically the Board Size, Board diversity, Board sub-Committees, Directors Educational Qualification and the frequency Board Meeting have a positive and significant impact on the bank Return on Asset (ROA).	0.0%	6.5%	0.0%	32.3%	61.3%	4.48	.811

Source: Own survey, 2020

As shown in the table 4.8 above, most of the board of directors strongly agreed that the bank had good improvement in its financial performance and the return on Assets has been improved during the last 5 years. The majority of the board of directors strongly agreed that the Corporate Governance practices of the bank board during the last five years has been improving and has significant contribution for the overall bank achievement and financial performance success specifically on Return on Asset (ROA).

Out of the total board of directors, 61.3% of them strongly agreed and believed that the Internal Corporate Governance mechanism of the existing board specifically the Board Size, Board diversity, Board sub-Committees, Directors Educational Qualification and the frequency Board Meeting have a positive and significant impact on the bank Return on Asset (ROA).

#### 4.4. Correlation Analysis

**Table 4.9 The relationship between independent and dependent variable**

			Correlations					
			ROA	BS	BD	BSC	BMD	NBM
Spearman's rho	ROA	Correlation Coefficient	1.000					
		Sig. (2-tailed)	.					
		N	31					
	BS	Correlation Coefficient	.468**	1.000				
		Sig. (2-tailed)	.008	.				
		N	31	31				
	BD	Correlation Coefficient	.499**	.117	1.000			
		Sig. (2-tailed)	.004	.530	.			
		N	31	31	31			
	BSC	Correlation Coefficient	.163	.154	.296	1.000		
		Sig. (2-tailed)	.380	.409	.106	.		
		N	31	31	31	31		
	BME	Correlation Coefficient	.561**	.468**	.349	.411*	1.000	
		Sig. (2-tailed)	.001	.008	.054	.021	.	
		N	31	31	31	31	31	
	NBM	Correlation Coefficient	.321	.319	.451*	.312	.504**	1.000
		Sig. (2-tailed)	.078	.080	.011	.087	.004	.
		N	31	31	31	31	31	31
**. Correlation is significant at the 0.01 level (2-tailed).								
*. Correlation is significant at the 0.05 level (2-tailed).								

Source: Own survey, 2020

As shown in the table 4.9 above the researcher conducted a Spearman correlation and study the correlation of the corporate governance variables. From the findings on the correlation analysis between Return on Assets and various predictors, the study found that there was positive correlation coefficient between Return On Assets and Board Size as shown by correlation factor of 0.468.

The study also found a positive correlation between ROA and Board Diversity as shown by correlation coefficient of 0.499. The association between ROA and Board Sub Committees found a positive relationship as shown by correlation coefficient of 0.163. The analysis also showed that the association between ROA and Board Members Education is positive relationship with correlation coefficient of 0.56. The association between ROA and Number of Meetings found positive relationship as shown by correlation coefficient of 0.321.

#### **4.5. Assumptions of Multiple Linear Regression**

For this study, the researcher has conducted analysis of the multiple linear regression key assumptions. As discussed below, the multiple regression assumptions tests conducted which includes the linear relationship between the outcome variable and the independent variables, Normality, Multicollinearity and Homoscedasticity.

##### **Linear Relationship**

In order to test the linearity assumption, the study examines the bivariate correlation for each pair of variables to make sure that linear correlation is detected. To test this, the research use Spearman two tailed test and the SPSS output shows that the Spearman correlation coefficients between all pairs of variables along with the significant level.

As it is explained in the above table 4.9 : Correlation Analysis , the study observed many significant correlations. The asterisks in table , one asterisk means the correlation is significant at the significant level of 0.05 and the two asterisk means the correlation is significant at the level of 0.01. The significant correlations indicate the linearly assumption. The linearity is apparent in this study.

##### **Normality of Data Test**

The normality tests for the variables were conducted with reference to the statistical data. To analyze and verify the normality, the Skewness and Kurtosis measures in SPSS are applied using statistical values and Std. Errors. The Skewness and Kurtosis Z-Values analyzed to verify whether the Z-Values are somewhere in the span of -1.96 to +1.96 after checking each categories of independent variables.

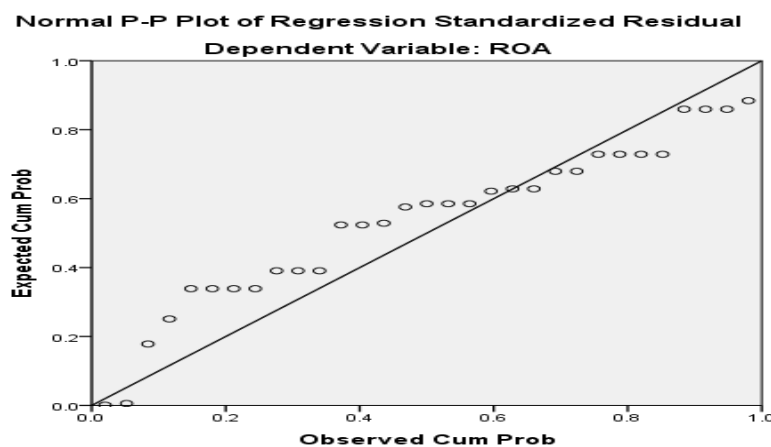
As per the below table 4.10 of SPSS statistical output, normality distribution of the dependent variable (ROA) for each categories of the independent variables( BS, BD, BME, NBM, ROA and BSC variables) were conducted.

The Skewness and Kurtosis Z-Values were analyzed by dividing the statistic measures of the skewness/kurtosis by its standard errors. As per the SPSS verification of the z-Values , the ROA is approximately normally distributed for independent variables. Hence ,it is assumed that the data are approximately normally distributed in terms of Skewness and Kurtosis z-Values.

**Table 4.10 Normality test**

Descriptive Statistics									
	N	Minimum	Maximum	Mean	Std. Deviation	Skewness		Kurtosis	
	Statistic	Statistic	Statistic	Statistic	Statistic	Statistic	Std. Error	Statistic	Std. Error
ROA	31	2.00	5.00	4.5161	.81121	-2.058	.421	2.376	.821
BS	31	4.00	5.00	4.2903	.46141	.672	.421	-1.134	.821
BD	31	3.00	5.00	4.3226	.59928	-.243	.421	-.537	.821
BSC	31	3.00	5.00	4.6774	.57079	-1.916	.421	2.161	.821
BMD	31	3.00	5.00	4.5806	.62044	-.221	.421	.557	.821
NBM	31	4.00	5.00	4.3226	.47519	.798	.421	-1.462	.821
Valid N (listwise)	31								

Also, as per the below normal regression output, the normal P-P plot we see a diagonal line and a bunch of little circles. The plot data is normal. The little circles follow the normality line, there is no drastic deviation.



**Figure 4.1: Normal Predicted Probability (P-P) plot**

## Multi-Collinearity

Multicollinearity can be detected with the help of tolerance and its reciprocal, called variance inflation factor (VIF). If the value of tolerance is less than 0.2 and, simultaneously, the value of VIF 10 and above, then the multicollinearity is problematic.

As per the rule, when tolerance value is less than 0.2 and the VIF exceeds 10; it is a signal of multi-collinearity, which could lead to misleading and/or inaccurate results. Multi-collinearity occurs when there are high inter-correlations among some set of the predictor variables. In other words, multi-Collinearity happens when two or more predictors contain much of the same information. As can be seen from below, the tolerance and VIF showed that there was no multi-collinearity because VIF of all variables were less than 10 and tolerance of all variables also greater than 0.2.

Coefficients <sup>a</sup>											
Model		Unstandardized Coefficients		Standardized Coefficients	T	Sig.	Correlations			Collinearity Statistics	
		B	Std. Error	Beta			Zero-order	Partial	Part	Tolerance	VIF
1	(Constant)	-.160	1.714		-.093	.926					
	BS	.645	.305	.367	2.113	.044	.388	.383	.346	.889	1.125
	BD	.541	.249	.400	2.176	.039	.400	.392	.356	.794	1.259
	BSC	.173	.245	.122	.707	.486	.228	.137	.116	.904	1.106
	NBM	-.286	.330	-.168	-.867	.394	.159	-.168	-.142	.715	1.398

a. Dependent Variable: ROA

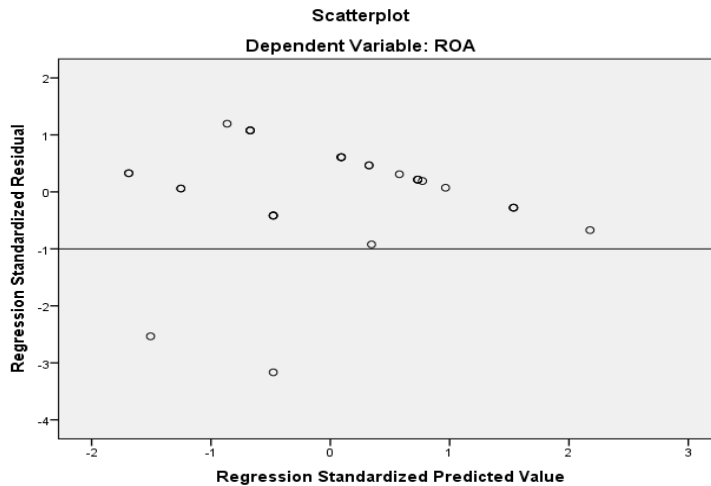
## Homoscedasticity Test

Homoscedasticity describes a situation in which the error term (that is, the “noise” or random disturbance in the relationship between the independent variables and the dependent variable) is the same across all values of the independent variables.

This assumption states that the variance of error terms is similar across the values of the independent variables. A plot of standardized residuals versus predicted values show whether points are equally distributed across all values of the independent variables.

In order to check the assumption of the homoscedasticity, the research used scatter plot technique. The below scatterplot of residuals versus predicted values used to check for

homoscedasticity. As illustrated in the figure, 4.1, below the graph looks like a random array dots or the plots have no pattern. There is no clear pattern in the distribution. It does not have a cone-shaped pattern. The data is homoscedastic. So, homoscedasticity assumption is not violated.



**Figure 4.2: Homoscedasticity test**

#### 4.6. Regression analysis

In order to see the influence of board size, board diversity, board sub-committee and number of board meeting on the bank’s return on asset, the study employed a multiple regression analysis. The study used Statistical Package for Social Sciences (SPSS Version 24) software to analyze the data by using multiple regression model.

**Table 4.11: Model summary**

Model Summary										
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Change Statistics					Durbin - Watson
					R Square Change	F Change	df1	df2	Sig. F Change	
1	.551 <sup>a</sup>	.303	.196	.72736	.303	2.829	4	26	.045	2.382
a. Predictors: (Constant), NBM, BSC, BS, BD										
b. Dependent Variable: ROA										

Source: Own survey, 2020

As shown in the Table 4.11 above, the value of adjusted R squared was 0.196; it means that there is a 19.6% of the impact of the independent variable (corporate governance variables) on the dependent variable (firm performance). It indicates that there was variation of 19.6% on the financial performance (ROA) of bank due to changes in Board Size, Board Diversity, Board Sub Committees and Number of Board Meetings at 95% confidence interval. This shows that 19.6% changes in financial performance of bank accounted for by Board size, Board Diversity, Board Sub Committees and Number of Board Meetings. R is the correlation coefficient which shows the relationship between the study variables. The ANOVA shows that there was a strong positive relationship between the study variables as shown by 0.551.

**Table 4.12: Analysis of variance**

ANOVA <sup>a</sup>						
Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	5.987	4	1.497	2.829	.045 <sup>b</sup>
	Residual	13.755	26	.529		
	Total	19.742	30			
a. Dependent Variable: ROA						
b. Predictors: (Constant), NBM, BSC, BS, BD						

Source: Own survey, 2020

As shown in the Table 4.12 above, the processed data, which is the population parameters, had a significance level of 0.055 which shows that the data is ideal for making a conclusion on the population's parameter as the value of significance (p-value) is less than 5%. The calculated was greater than the critical value ( $2.262 < 2.829$ ) an indication that Board size, Board diversity, Board Sub Committees and Number of Board Meetings were significantly influencing financial performance (ROA) of Zemen Bank. The significance value was less than 0.05 an indication that the model was statistically significant.

**Table 4.13: Coefficients**

Coefficients <sup>a</sup>											
Model		Unstandardized Coefficients		Standardized Coefficients	T	Sig.	Correlations			Collinearity Statistics	
		B	Std. Error	Beta			Zero-order	Partial	Part	Tolerance	VIF
1	(Constant)	-.160	1.714		-.093	.926					
	BS	.645	.305	.367	2.113	.044	.388	.383	.346	.889	1.125
	BD	.541	.249	.400	2.176	.039	.400	.392	.356	.794	1.259
	BSC	.173	.245	.122	.707	.486	.228	.137	.116	.904	1.106
	NBM	-.286	.330	-.168	-.867	.394	.159	-.168	-.142	.715	1.398

a. Dependent Variable: ROA

Source: Own survey, 2020

From the data in the above table 4.13 , the established regression equation was

$$ROA = -0.160 + 0.645BS + 0.541BD + 0.173BSC - 0.286NBM$$

As shown in the Table 4.12 above, the multiple regression analysis revealed that Board Size, Board Diversity, Board Sub Committees and Number of Board Meetings to a constant zero, financial performance of bank would stand at 0.160 , a unit increase in board size would lead to decrease in financial performance (ROA) of the bank by a factor of 0.645, unit increase in Board diversity would lead to increase in financial performance of the bank by a factor of 0.541 , a unit increase in Board Sub Committees would lead to increase in financial performance of the bank by a factor of 0.173 and unit increase in Number of Board meeting would lead to decrease in financial performance of the bank by a factor of 0.286.

At 5% level of significance and 95% level of confidence, Board Size found significant impact of corporate governance of the Zemen bank ( $p = 0.044$ ). Thus, hypothesis1: There is a statistical relationship between Board size and Bank Financial Performance (ROA), was accepted.

Board Diversity found significant impact on corporate governance of Zemen bank ( $p=0.039$ ). Thus, hypothesis 2: There is a statistical relationship between Board diversity and Bank Financial Performance was accepted.

Board Sub Committees found insignificant impact on corporate governance of the bank ( $p=0.486$ ). Thus, hypothesis 3: There is a statistical relationship between Board sub-committees and Bank Financial Performance (ROA) was rejected.

Number of Board Meeting found insignificant impact on the corporate governance of the bank ( $p>0.05$ ). Thus, hypothesis 4: There is a statistical relationship between Board members' educational qualification and Bank Financial Performance (ROA) was rejected.

To check the presence of multi-collinearity, the study employed the VIF for the independent variables. It denotes that the VIF value for each independent variable is insignificant and less than ten which indicates the estimated result of the model for ROA concerning the independent variables Board size, Board Diversity, Board Sub Committee and Number of Board Meeting are free from multi-collinearity except Board Members Education which was excluded from the model as the VIF result was above the tolerance rate.

Finally, in terms of the Multiple Regression analysis, the study comes to conclude that the predictors' power on the corporate governance has less impact. The results of the regression analysis summarized in above tables show that corporate governance contributes significantly to the firm performance ( $F=2.829$ ;  $P<0.05$ ) and predicts 19.6 percent of the variation found.

#### **4.7. Qualitative Data Analysis**

##### **What are the major strengths of the bank board?**

*“The bank board members/ directors are professional, confident and the right personnel at the right post. They are the key players and direct the bank to the right directions”* (Board member, personal communication, October 26, 2020).

*“The board of directors of the bank are professionals from different disciplines and qualified directors. I know most of the board directors have amazing work experience from big organizations in the country”* (Board member, personal communication, October 25, 2020).

*“The diversity, experience and relevant qualifications in some areas that are key to the bank at the current moment, for example, a member with a civil engineering background has been a very good mix to the composition of the members in advancing the bank’s new building project including making the needed adjustments that were identified after the current members joined the board”* (Board member, personal communication, October 25, 2020).

### **How could the board governance be improved?**

*“Strengthening of the board room with additional manpower in maintaining and building the information system could enhance the efficiency of the board governance”.* (Board member, personal communication, October 25, 2020).

*“Strict implementation of the national bank directives, the bank policy and procedure, establishment and approval of the bank senior management code of conduct (which is in the pipeline); providing training to the board of directors and the bank management on risk identification and mitigation, internal control, strategy development and on good governance etc. promoting transparency across the bank board room”* (Board member, personal communication, October 25, 2020).

*“Policy governance is the core, transparency, accountability, feedback, regular and extraordinary meetings for timely decision. The board overall corporate governance can also be more efficient if they can accommodate young professionals. The board of directors should understand the current banking environment and practices of other competing banks. The board of directors should work to be best banking the country. They can bring new banking and governance practices from the international banking environment. Work towards the international corporate governance standards and practices. The board must work to evaluate the corporate governance practices of the bank on periodic basis.* (Board member, personal communication, October 25, 2020).

### **Do you feel that the bank is headed in the right direction?**

*“It is heading in the right direction with its business model in terms of limited branches and high tech based and efficient services including diversifying its business focus and reducing the concentration and becoming more inclusive in the cliental profile will*

*enable it to be a leader in the industry” (Board member, personal communication, October 25, 2020).*

*“In all most bank performance measurement parameters such as deposit, loan, income, foreign currency generation return on asset, etc the bank has been registering remarkable growth and performance year after year; 30% and above” (Board member, personal communication, October 26, 2020).*

*“The bank is unique because of its strategy it is innovative bank. Gives good focus for customer satisfaction, develop, and motivates human capital. Growing fast, good return on capital and return on asset, good reputation. It is heading in the right direction because its growth trajectory is upward for the last three years more than the previous periods. The bank is on the right track and will achieve more. It is one of the competing banks in the industry with various innovative ideas and banking service. (Board member, personal communication, October 25, 2020).*

*“The bank is headed in the right direction. In the past eight months, the board has conducted meetings at least twice a month. Moreover, the board committees have conducted several meetings with relevant departments of the bank and the CEO. All these have created excellent working relationship between the board and the management. As a result, positive achievements have been registered in the areas of cost reduction, capacity building, strategic directions and reduction of non-performing loan (NPLs). To mention, but few, the NPL of the bank, which was above the National Bank’s limit of 5% is now 3.3%. Additional branch offices are opened in strategic locations. More employment opportunities are generated. Introduction of a modern information technology, which is believed to improve the services and competitiveness of the bank in the marketplace and generate additional revenue, is underway. Revenue of the bank shows a steady growth trend. (Board member, personal communication, October 24, 2020).*

**In your opinion, what are the major corporate governance problems or issues faced by the bank?**

*“With the increasing competitive environment in the industry, the bank has been facing challenges in maintaining the staffing and key personnel given the imbalance on the*

*supply and demand for experienced personnel in the market in which competing banks take one another's personnel with better salary and benefits, etc. The bank has recognized the challenge and begun to address the problem through immediate adjustments against the industry and will in the long-term address through the upcoming five-year strategic plan and ten-year long-term strategy and associated new process and structure” (Board member, personal communication, October 25, 2020).*

*“Lack of effective governance are among the most important internal factors which may endanger the solvency of the bank. The board members are somehow busy with their other engagement and somehow affects their fullest commitment and not to engage and deliver more” (Board member, personal communication, October 26, 2020).*

*“Sometimes, there are misunderstanding of the board roles in the industry and the bank is not an exception. The board room must give chance and should work to incorporate young professionals as it will help the bank cultivate successors of the bank. I believe that the board can deliver and score better result if they continue with current level of commitment and professionalism. Train the board of directors with new and practical corporate governance principles”. (Board member, personal communication, October 24, 2020).*

*“The bank board members have to prepare for the competing bank industry as new banks are coming to the market and to compete with the existing banks to maintain and earn more market share. As the new transition and reform government has shown its plan and becoming flexible to open the bank market for international bank operators, as this brings opportunity and threat for the new banking environment” (Board member, personal communication, October 25, 2020).*

*“The board will be replaced as per the decision of the general assembly on periodic bases that helps to give chance for others qualified professionals to contribute for the bank. I will also advise the board can implement new practices to evaluate or assess the board members' performance on periodic basis during their terms” (Board member, personal communication, October 26, 2020).*

*“The bank board has to work towards the international corporate governance standards and practices. The board must work to evaluate the corporate governance practices of*

*the bank on periodic basis” (Board member, personal communication, October 25, 2020).*

*“In business, corporate governance is associated with sustainable development. Impressive economic performances coupled with high net profit measured by acceptable economic parameters are the primary objective of any commercial bank. This means, the primary focus is maximizing profit. However, in order to achieve their goals commercial banks, including Zemen bank should strictly adhere to the benefits. Sociocultural and environmental concerns cannot be ignored. Ignoring such concerns is detrimental to the very existence of business in general and the banking business. That is why corporate social and environmental responsibilities are encouraged. This is all about principles of corporate governance. (Board member, personal communication, October 24, 2020).*

## CHAPTER FIVE

### CONCLUSIONS AND RECOMMENDATIONS

The previous chapter contained the data analysis and the findings of the study. This chapter of the study contains the conclusions drawn and the recommendations given based on the major findings in the previous chapter.

#### 5.1 Conclusion

The study examines the relationship between corporate governance and financial performance for the period of five years from the year 2010 to 2019. The researcher drawn the following conclusions based on the result of the data analysis.

Based on the descriptive statistics the existing board size is the idea and perfect size recommended for any bank board. The size is in accordance with the National Bank of Ethiopia directive within the range of maximum and minimum number of board members. The existing board has sufficient size and composition to perform its role and responsibilities without due disruption. The board has sufficient size so that, there are sufficient board members to discharge the board's workload. Most of the directors believe that the existing board size is large enough and the board room is benefiting from larger boards as it gets diversified expert advice and opinions around the table compared to a small board. The board size is large enough and expected to increase board diversity in relation to experience, skills, gender and the bank financial performance (ROA). Bank has established recommendable board size with board members that have adequate skills and competencies to carry out their responsibilities. The numbers of board members are not too many members; hence board members' discussions are not constrained, and all board members are meaningfully engaged in and contribute to deliberations. The board size has helped the board members to establish ease of interpersonal relations at the board table. The board members and its size are manageable. Directors do not face challenge to know their fellow board members and, to gain trust & confidence in them.

Most of the respondents rated agree on their opinion about increasing the existing board size if it may have a positive and significant impact on the bank financial performance (ROA). In line with this, the member of the board feel that the existing bank board has moderate size as

it does not affect the board productivity, its communication and board decision making process. The board members believe that the larger board members may have impact on the bank board capacity for monitoring role and will result in poorer communication and decision- making interruption. The boards of directors also believe that the bank board size should not be small as they also believe that small board size has impact to promote critical, genuine, and intellectual deliberation, which presumably lead to ineffective corporate decision- making process.

The bank board has a diversified and well-balanced board of directors with as various attributes, such as age, gender, ethnicity, career, and work life experiences. The diversity in the boardroom increases board independence and improves executive monitoring. The board members' diversity brings diversity in ideas, perspectives, experiences, and business knowledge to the decision-making process in boardrooms. The board diversity also increased creativity and innovation in boardrooms due to diversity in reasoning abilities, which can also facilitate effective decision-making. The director and members of the board room believe that diversity as a positive force, the existence of multiple and divergent viewpoints within a board significantly enhance the bank financial performance (ROA). The board room is gender diversified but not well balanced. It has Women directors who are committed, respected and professionals, and their influence to the board decisions increases with their numbers.

The diversity of the board directors helps to improve the bank and its financial performance as it links the bank to screen the external environment from different perspectives that emanate from the diversified board members including board members skills, business contacts, reputation & business opportunities. The diversity of the bank board has no negative impact on the effective monitoring and decision-making of the board room. The more diversity of the board members is well appreciated, and it does not disrupt the board room performance by bringing the individual interests to the board that inhibit boardroom cohesion and overall financial performance of the bank.

The bank board room has established audit subcommittee, risk management and compliance sub-committee and human resource affairs sub-committee. The board sub committees have played significant role and improved the bank corporate governance as the main board delegate specific tasks to the board subcommittee and utilizing the contribution of non-executive directors. The Audit Sub-Committee provides independent oversight of the bank's financial reporting and internal control system and ensures checks and balances within the

bank. The Risk Management and Compliance Sub-Committee oversees senior management's activities in managing credit, market, liquidity, operational, legal, and other risk and ensure that the risk management process is in place and functioning. The Human Resource Affairs Sub-Committee provides formal and transparent proposal on the employment and replacement of senior management members and on the overall compensation. The boards of directors believe that the effectiveness of the board is influenced by board committees as the regulatory recommendations and the complexity of bank activities place emphasis on the importance of board committees. The bank board uses the above-board sub- committee structures to facilitate, evaluate, and ratify long-term investment decisions and to monitor the performance of senior management. The boards of directors believe that the different board sub-committees have a positive and significant impact on the Financial Performance of the bank.

The bank board comprise of directors who has a mixture of core competencies such as banking, finance, accounting, management, economics, Engineering, legal, business administration, auditing information technology and investment management. The bank board room has directors with well qualified and ranked educational qualifications and contributed for the board room performance and to achieve better result from the strategic decision-making. The existence of qualified directors in the bank board room has increased the bank performance as they promote corporate image and demonstrate accountability and credibility within the team. The bank board room plays an important role in formulating and implementing business strategy as it is composed of directors who bringing expertise and knowledge. The bank board has directors with diversified skills that can assess the internal business conditions and scan the external environment properly in running the bank business successfully. The bank board members believe that the educational qualification of the existing board room has a positive and significant impact on the Zemen bank Financial Performance. On the other hand, the board directors highly emphasize board members work and life experience linkage with educational qualification for the bank existing and future success.

The intensity of board activity is measured by the frequency of board meetings as it indicates the board commitment and monitoring role of the board. The bank board meetings create opportunity for the board members to come together, to discuss and exchange ideas about the progress of their strategy and monitoring role in a timely manner. It has been observed that

the board meeting time is adequate and has significant contribution for improving the effectiveness of the bank board and overall bank financial performance (ROA). The bank board members are meeting more frequently beyond their regular schedule meeting and it has contributed more to improve board performance, track their performance, and tends to improve the bank financial performance (ROA). The boards of directors believe that increasing the level of board activity through board meetings lead to better bank achievement and financial performance. The bank board members well aware and committed to attend in person at least 75% of the board meetings within the financial year as per the regulation. The current practice of the board meetings is conducted at least once in a month in the Zemen Bank Head Office in accordance with the rules for conducting board meetings. The frequency of the board meeting has helped board members to bring their concern to the board table and to have enough time to discuss on strategic manager with due care. This has also observed as positive impact and contribution for the bank financial performance (ROA). Most of the bank board directors believe that frequent board meeting has a positive and significant impact on the bank financial performance (ROA). In general, the board directors believe that frequent board meetings are useful and recommended for directors to exchange meaningful ideas among themselves.

Based on the correlation analysis, most of the corporate governance mechanisms (board size, board diversity and board members' educational qualification) were found significantly correlated with the financial performance of the bank.

Based on the regression analysis, the board size was found to have a positive and significant impact on the financial performance of the bank. The big board size is effective to improve financial performance of the bank. This result is in line with the research.

Board diversity was found to have a positive and significant influence on the financial performance of the bank. The presence of women board directors is also important for the financial performance of the bank. Therefore, the role of women's in the board or top position of the bank has positive impact on the board performance. This result is in line with the research.

Board sub-committee was found to have a positive but insignificant impact on the financial performance of the bank. This result is not in line with the research proposal.

Number of board meeting was found to have a negative but insignificant impact on the financial performance of the bank. This result is not in line with the research proposal.

Based on the qualitative data analysis, the Zemen bank boards of directors are professionals from different disciplines and qualified directors. The board governance could be improved more by providing training to the board of directors on specialized topics including risk identification and mitigation, internal control, strategy development and on good governance. Almost all of the board members believe that the organization is headed in the right direction. However, the concerns of the board of directors are also noticed. It is also commented that the increasing competitive environment in the bank industry will be challenging for the Zemen bank as maintaining the staffing and key personnel given the imbalance on the supply and demand for experienced personnel. The board of directors clearly stated that the banking industry and market is experiencing tough competition by migrating top bank officials including Bank Presidents from one bank to other from one with better salary and benefits. This is serious problem and one of the major challenges in the corporate governance practices of the bank.

## **5.2. Recommendation**

Based on the conclusions drawn above, the study recommends that stakeholders of the bank should take in to account the corporate governance variables i.e., board diversity when electing board of directors for board room.

### **❖ Well balanced board diversity**

The board room need to have reasonable and well-balanced board of directors with various attributes including age, gender, ethnicity, religion, work career and life experiences. The diversity of the board members brings diversity in ideas, perspectives, experiences, and business knowledge to the decision-making process. The diversity in the boardroom increases the board room creativity and innovation as the directors bring diverse viewpoints and reasoning abilities that increase board independency and improves executive monitoring.

Based on the research findings, the study noticed that most of the Zemen bank boards of directors are male and the board is room is male dominated. Based on the research, Zemen

bank is advised to ensure and maintain the well representation of both gender in the board room.

Now a days most of successful business are witnessing and favoring diversity of board room in different perspectives. Gender diversity on the board of companies is a growing fact and necessity to be competent and successful in the business industry. Even though the progress made by women in their education qualification, exhibit commitment and motivation in the business world, the fact on the ground still shows that gender diversity and women continue to be under-represented in decision-making.

The Zemen bank is advised to exploit the underutilized pool of qualified, experienced, competent, and motivated women available among the shareholders that can enhance, improve, and bring diversity of thought to the boardroom, thus strengthening the Zemen Bank competitive advantage.

#### ❖ **Board Size Increment**

Based on the research findings, the study recommended that; special attention should be given when deciding and dealing with the number of board members. As per the National Bank of Ethiopia Directive, Bank Corporate Governance Directive SBB/71/2019, a bank shall have at least nine directors. The Zemen bank board sizes is in accordance with the National Bank of Ethiopia directive and meet the minimum number of board members. The existing board room has nine board of directors.

The first hypothesis tested evidenced that there was a statistically significant and positive relationship between the Zemen bank board size and the bank financial performance (ROA).

Even though the existing board size is the ideal and meet the minimum number of the national bank recommendation, from the research finding it is noticed that the positive relation of the Zemen bank board size with the financial performance. Hence there is room the bank to consider increasing the bank board size.

The Zemen bank also advised to consider the positive implication of increasing the board size to the reasonable size as increasing the board size to ideal level will benefit the advantage of

larger board to get diversified expert advice and opinion around the table compared to a small board.

The Zemen bank should ensure that the board size not to be too large. The bank should ensure that the increased board members number benefit outweighed the incremental cost of poor communication and decision-making interruption.

In general, the size of the board should match with the size of the bank to avoid scenarios of having too small boards which will be overburden and constrained board members not meaningfully engaged in and contribute to deliberations, and board Size should not be too large as that make the board unproductive with ineffective communication and delay the board room decision making process that led to inefficient and underperforming board room.

#### ❖ **Board Room Performance Evaluation**

In addition to the above recommendations based on the about two key corporate governance variables (Board Size and Board Diversity), the research has also noticed the importance of board performance evaluation and corporate governance rating of the bank. The researcher wants to bring this to the bank shareholder attention the benefit the Zemen bank obtain from conducting periodic performance evaluation of the board room and board of directors.

As it is believed by behavioral psychologists and organizational learning experts agree that people and organizations cannot learn without feedback. No matter how good a board is, it's required to get better if it's reviewed and evaluated based on the annual strategic plan and schedule.

The National bank of Ethiopia is the regulatory body that issues different Directives to provide guidelines to ensure banks are soundly and prudently managed and directed. The annual reporting and monitoring of the board performance is performed by the National Bank of Ethiopia. However, the researcher recommends this annual reporting and evaluation of the board has to be made in well structure and result based evaluation approach. The shareholders should consider the importance of board room evaluation and should be considered as one of the major reports to be presented in the Shareholder annual General meeting.

The board room performance review or evaluation can do in different format which include Board room Evaluation, Individual self-assessment of director and Peer reviews of Directors.

#### ❖ **Conduct Bank Corporate Governance Rating**

The research is also like to bring to the attention of the Zemen Bank shareholders and Board of directors and recommend the Zemen bank to conduct the Bank Corporate Governance Rating by external rating company or from other professional firm about the status of the Zemen bank corporate governance practices. It helps the shareholders to manage their share in the bank and other stakeholders for their future investment decision as they can differentiate and know the status of the Zemen bank based on the bank corporate governance practices and performance.

#### ❖ **Board Members tailored Corporate Governance Training**

From the qualitative data analysis and findings, the researcher has found and noticed that Zemen bank boards of directors are professionals from different disciplines and qualified directors. The board governance could be improved more by providing training to the board of directors on specialized topics including risk identification and mitigation, internal control, strategy development and on good governance.

The researcher recommended the board room to be provided a structured and directors tailored Corporate governance training to improve the board members knowledge based on the internationally accepted corporate governance principles (OECD Principles, the Basel guidelines, Cadbury Committee guidelines and other Corporate Governance best practices).

The training will help the board members to be familiar with the recent Corporate governance best practices and offer guidelines to be most effective in bringing strategic value to their bank and the board plays a key role for the Zemen bank success when they develop strong understanding of, and successfully implement, corporate governance best practices.

### **5.3. Research Contributions**

The empirical findings on corporate governance indicated inconclusive relationships between the corporate governance and its impact on the financial performance of banks.

Most of the previous studies had information inaccessibility from the board of directors and board rooms. As it was explained in the first chapter under the rationale of the study, the research is one of the shareholders of the Zemen Bank Share Company. This research paper prepared based on the first-hand information from the board room and board of directors.

This research has also contributed to improving the existing literature and corporate governance variables i.e., board size and board diversity. The research finding has validated the comprehensive conceptual framework. The quantitative data analysis based on the regression analysis showed that the board size has positive and significant impact on the financial performance of the bank. The findings also indicated a positive and significant relationship between board diversity and the financial performance of the bank. The researcher conducted an independent assessment of the Zemen bank corporate governance practices. The research finding provides information that benefits the shareholders and other stakeholders for their future investment decision. It helps shareholders to manage their shareholding in the bank as they can differentiate the status of the bank based on the bank corporate governance practices.

The focus of this research was on one of the Ethiopian private commercial banks. The importance of this Corporate governance research explained by the limited knowledge about the corporate governance practices in the private bank sectors in Ethiopia. The importance of this research is also described by the inconsistent results of the previous studies about the corporate governance practices and its impact on the performance of banks in Ethiopia.

The empirical study of the corporate governance practice showed that most of the studies are for developed country and its significance is limited for countries like Ethiopia because of the differences in the social set up, cultural values and economic conditions compared to developed economies. This research brings new findings by assessing the corporate governance practices and its impact on the bank financial performance (ROA) with a focus on one of the private banks in Ethiopia, Zemen Bank Share Company.

Most of the previous researches were conducted on the Government owned banks including Commercial Bank of Ethiopia and Construction Bank of Ethiopia focusing only on the assessment of the corporate governance practices. This research has suggested corporate governance models unique to the private commercial bank.

This research examines the existing corporate governance practices according to the National Bank of Ethiopia (NBE) and internationally accepted organizations including OECD (Organization for Economic Co-operation and Development). It forwards recommendations and best practices that improve the current practices. Thus, this provides the incentive for other student researcher to aim to contribute and narrow the knowledge gap in this area.

#### **5.4 Limitations of the Study**

The descriptive research design adopted for this study which includes questionnaires, observation method and interviews. The limitations that are associated with all these methods apply to this study.

This research focuses on one of the private commercial banks operating in Ethiopia, Zemen Bank S.C, to assess the Corporate Governance practices and its impact on the financial performances. There are limited sources of data and access restriction to the banks databases due to the banks confidentiality policy. Data collected for research may also contain errors, or biasness from the respondents.

The reference documents used during the literature review largely focused more on developed economies than developing economies like Ethiopia.

The study has used the internationally accepted organizations principle (OECD Principles, the Basel guidelines, Cadbury Committee guidelines and other Corporate Governance best practices) to benchmark the corporate governance practices of Zemen bank S.C as Ethiopia has no standard codes of corporate governance against which corporate governance practices of companies can be assessed.

The current world pandemic- COVID 19 situation and time can also be mentioned as constraints due to people movement restriction and respondent's unavailability to get information. It is also difficult to get timely feedback from responds as most of the respondents are board members and top bank officials. The boards of directors were busy to take part in the study.

## **5.5 Implications for Future Research**

There are several ways in which this research can be expanded. Based on the results of this study, some future research work is recommended. The results of this study indicate opportunities for future research.

The sample drawn was restricted to assessing the corporate governance practices of the Zemen bank and its impact on the financial performance of the bank. This has to be extended to other private banks to have a broader perspective on the corporate governance practices and its impact on the banks financial performance and validate the results.

There is also the need for further development of theory in corporate governance as that would lead to developing more holistic models for corporate governance of commercial banks in Ethiopia. This research paper identifies the direction for future research which should become the basis for guiding the next generation of effective corporate governance reforms.

The research finding on Corporate Governance practices in one of the private banks is impressing as it will help Board of directors, bank supervisors, and regulators to frame policies. The study also offers reliable and valid research instruments than can be used by other researchers for similar purposes.

In the view of the above all, the research contributes its share to the literature in general for Corporate Governance practices and specifically for the development of the private banking sector in Ethiopia. It tries to identify the best Corporate Governance practices that can contribute and improved the profitability of private commercial banks.

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## APPENDIX

### ANNEX I: Corporate Governance Practice Questionnaire-Board Secretary

#### ZEMEN BANK SHARE COMPANY

#### CORPORATE GOVERNANCE PRACTICE QUESTIONNAIRE

**Dear Board Secretary,**

Thank you very much for your willingness to take time to respond to this research questionnaire.

My name is Wossenu Abera. I am attending the Executive MBA program at Addis Ababa University, College of Business and Economics. I am currently conducting a research on the Corporate Governance Practices of Zemen Bank Share Company as a partial fulfillment of the requirements for Master's in Business Administration Degree.

Attached you will find a questionnaire prepared only for the purpose of gathering information about the Corporate Governance Practices in the Zemen Bank Share Company. This questionnaire is prepared only for the purpose of gathering information.

You are kindly requested to participate in this survey which would not take more than 10 minutes. Your responses will be kept strictly confidential.

Should you have any questions or concerns regarding completing the questionnaire, please call 0911 22 53 05 or email to [aberaw@unaid.org](mailto:aberaw@unaid.org).

Thank you in advance for your time and effort in completing this survey questionnaire.

Best regards,

Wossenu ABERA

#### Anonymity Guarantee

Your responses to this Corporate Governance assessment are anonymous. It is assured that the data furnished, and the identity of the respondents will be kept strictly confidential.

*Thank you for your time!!!*

**Instruction:** Please fill in for the questions listed below.

**Question 1 BOARD SIZE & DIVERSITY**

<b>Year</b>	<b>Total number of board members</b>	<b>Total number of female boards Members</b>
<b>2010</b>	8	1
<b>2011</b>	9	1
<b>2012</b>	8	1
<b>2013</b>	9	2
<b>2014</b>	9	2
<b>2015</b>	9	2
<b>2016</b>	9	2
<b>2017</b>	9	2
<b>2018</b>	9	2
<b>2019</b>	9	2

**Question 2 BOARD MEETINGS**

<b>Year</b>	<b>Number of boards Meetings</b>	<b>Number of sub committee meetings</b>	<b>Number of board sub-committees</b>	<b>Name of board sub- committees</b>
<b>2010</b>	24	36	4	Human Resource, Risk, Audit, Loan Review
<b>2011</b>	24	36	4	Human Resource, Risk, Audit, Loan Review
<b>2012</b>	24	36	4	Human Resource, Risk, Audit, Loan Review
<b>2013</b>	24	36	4	Human Resource, Risk, Audit, Loan Review
<b>2014</b>	24	40	4	Human Resource, Risk, Audit, Loan Review
<b>2015</b>	24	40	4	Human Resource, Risk, Audit, Loan Review
<b>2016</b>	24	67	7	Human Resource, Risk, Audit, IT, Strategy & Budget, HQ building, Loan Review
<b>2017</b>	24	67	7	Human Resource, Risk, Audit, IT, Strategy & Budget, HQ building, Loan Review
<b>2018</b>	26	67	7	Human Resource, Risk, Audit, IT, Strategy & Budget, HQ building, Loan Review
<b>2019</b>	26	67	7	Human Resource, Risk, Audit, IT, Strategy & Budget, HQ building, Loan Review

**Question 3- BOARD MEMEBERS EDUCATIONAL QUALIFICATIONS**

Year	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
<b>Academic qualification in</b>	<b>Number of board members</b>									
Finance	√	√	√	√	√	√	√	√	√	√
Accounting	√	√	√	√	√	√	√	√	√	√
Banking	√	√	√	√	√	√	√	√	√	√
Auditing	√	√	√	√	√	√	√	√	√	√
Economics	√	√	√	√	√	√	√	√	√	√
Business Management	√	√	√	√	√	√	√	√	√	√
Law	√	√	√	√	√	√	√	√	√	√
Information Technology								√	√	√
Investment Management										
Other								√	√	√
<b>Total number of Board members</b>	8	9	8	9	9	9	9	9	9	9

**Question 4- FINACIAL PERFORMANCE (Return ON Asset)**

Year	Profit Before tax in ETB	Total Asset	Return on assets (Profit Before Tax/Average Total Assets)
<b>2010</b>	59,995,141	1,055,622,793	0.057
<b>2011</b>	121,132,619	1,613,912,451	0.075
<b>2012</b>	123,311,926	2,394,242,097	0.052
<b>2013</b>	123,810,853	3,248,457,497	0.038
<b>2014</b>	165,017,423	3,924,769,457	0.042
<b>2015</b>	200,924,631	4,874,340,646	0.041
<b>2016</b>	270,051,307	7,374,131,617	0.037
<b>2017</b>	368,432,000	9,756,518,000	0.038
<b>2018</b>	342,319,000	12,489,150,000	0.027
<b>2019</b>	635,856,000	14,689,021,000	0.043

**Thank you for your time!**

**ANNEX II: Corporate Governance Practice Questionnaire-Board Director**

**Zemen Bank Share Company**

**Corporate Governance Practice Questionnaire**

**Dear Director,**

Thank you very much for your willingness to take time to respond to this research questionnaire.

My name is Wossenu Abera. I am attending the Executive MBA program at Addis Ababa University, College of Business and Economics. I am currently conducting a research on the Corporate Governance Practices of Zemen Bank Share Company as a partial fulfillment of the requirements for Master's in Business Administration Degree.

Attached you will find a questionnaire prepared only for the purpose of gathering information about the Corporate Governance Practices in the Zemen Bank Share Company. This questionnaire is prepared only for the purpose of gathering information.

You are kindly requested to participate in this survey which would not take more than 10 minutes. Your responses will be kept strictly confidential.

Should you have any questions or concerns regarding completing the questionnaire, please call 0911 22 53 05 or email to [aberaw@unaid.org](mailto:aberaw@unaid.org)

Thank you in advance for your time and effort in completing this survey questionnaire.

Best regards,

Wossenu Abera

**Anonymity Guarantee**

Your responses to this Corporate Governance assessment are anonymous. It is assured that the data furnished, and the identity of the respondents will be kept strictly confidential.

*Thank you for your time!!!*

Please answer every item putting a tick (✓) mark as appropriate and feel free to make additional comments.

**SECTION ONE: PERSONAL PROFILE**

1. **Gender:** Male \_\_\_\_\_ Female \_\_\_\_\_
2. **Age group:**  
 30-39 \_\_\_\_\_ 40-49 \_\_\_\_\_ 50-59 \_\_\_\_\_ Over 50 \_\_\_\_\_
3. **Work experience** in the same business, related or other  
 1-5 Years \_\_\_\_\_ 6-10 years \_\_\_\_\_ 11-15 years \_\_\_\_\_  
 16-20 years \_\_\_\_\_ 21 & more \_\_\_\_\_
4. **Highest level of education**  
 Certificate \_\_\_\_\_ Diploma \_\_\_\_\_ Bachelor's Degree \_\_\_\_\_  
 Master's Degree \_\_\_\_\_ Doctoral Degree \_\_\_\_\_ Other (Please Specify) \_\_\_\_\_
5. **Major background (Field of study):** \_\_\_\_\_

**SECTION TWO: RATING**

Please use the following scale in rating the Board's performance. Place an (✓) in the appropriate box.

Rating Scale:

**Level 5:** I *strongly agree* with this statement. The board *always* practices this as a part of its governance responsibilities. The board's performance in this area is *outstanding*.

**Level 4:** I *Agree* with this statement. The board *usually* practices this as a part of its governance responsibilities, but not always. The board performs *well* in this area.

**Level 3:** I *Neutral* with this statement. The board *often* practices this as a part of its governance responsibilities but is not consistent. The board performs *fairly well* in this area.

**Level 2:** I *Disagree* with this statement. The board *inconsistently* practices this as a part of its governance responsibilities. It *does not perform well* in this area.

**Level 1:** I *Strongly disagree* with this statement. The board *never* practices this as a part of its governance responsibilities. It performs *poorly* in this area.

I	BOARD SIZE: Listed below are some characteristics that describe a Board Size. How would you rate the Board on the following?	1 Strongly disagree	2 Disagree	3 Neutral	4 Agree	5 Strongly agree
1.1	The existing board size is the idea and perfect size recommended for any bank board. The size is in accordance with the National Bank					

	of Ethiopia directive within the range of maximum and minimum number of board members.					
1.2	The existing board has sufficient size and composition to perform its role and responsibilities without due disruption.					
1.3	As a member of the board, you feel that the existing bank board has too many directors that make the board unproductive with ineffective communication and delayed the board decision making process.					
1.4	The bank board capacity for monitoring increases as more directors are added, and the increased board members number benefit outweighed the incremental cost of poorer communication and decision- making interruption.					
1.5	As one of the board of directors, you believe that the bank board size should be small to promote critical, genuine, and intellectual deliberation and involvement among members, which presumably lead to effective corporate decision- making, monitoring and improved performance.					
1.6	The board has sufficient size so that, there are sufficient board members to discharge the board's workload.					
1.7	As director you believe that the existing board size is not large enough and the board room is benefiting the advantage of larger boards to get diversified expert advice and opinions around the table compared to a small board.					
1.8	The board size is not large enough and expected to increase board diversity in relation to experience, skills, gender and the bank financial performance(ROA).					
1.9	Bank has established recommendable board size with board members that has adequate skills and competencies to carry out their responsibilities.					

	1	2	3	4	5
	Strongly disagree	Disagree	Neutral	Agree	Strongly agree
1.10 The number of board members are not too many members; hence board members discussions are not constrained, and all board members are meaningfully engaged in and contribute to deliberations.					
1.11 The board size has helped the board members to establish ease of interpersonal relations at the board table.					
1.12 The board members and its size are manageable. Directors do not face challenge to know their fellow board members and, to gain trust & confidence in them.					
1.13 As a member of the board room, you believe that increasing the existing board size has a positive and significant impact on the bank Financial Performance(ROA).					

**BOARD SIZE: Any other Comments or suggestions.**

II	BOARD DIVERSITY	1	2	3	4	5
	Below are listed some characteristics that describe Board Diversity. How would you rate the Board on each of the following?	Strongly disagree	Disagree	Neutral	Agree	Strongly Agree
2.1	The bank board has a diversified and well-balanced board of directors with as various attributes, such as age, gender, ethnicity, culture, religion, independence, career, and life experiences.					
2.2	The diversity in the boardroom increases board independence and improves executive monitoring.					
2.3	The board members diversity brings diversity in ideas, perspectives, experiences, and business knowledge to the decision-making process in boardrooms.					
2.4	The board diversity also increased creativity and innovation in boardrooms due to diversity in reasoning abilities, which can also facilitate effective decision-making.					

	1 Strongly disagree	2 Disagree	3 Neutral	4 Agree	5 Strongly Agree
2.5 As a director and members of the board room, you believe that diversity as a positive force, the existence of multiple and divergent viewpoints within a board significantly enhance the bank financial performance(ROA).					
2.6 The board room is gender diversified and has Women directors who have better oversight, and their influence on the board decisions increases with their numbers.					
2.7 The diversity of the board directors helps to improve the bank and its financial performance as it links the bank to its external environment and secure critical resources, including skills, business contacts, reputation & business opportunities.					
2.8 The diversity of the bank board has negative impact on the effective monitoring and decision-making of the board room.					
2.9 The more diverse board members bring their individual interests and commitments to the board that inhibit boardroom cohesion and impacted the overall financial performance of the bank.					

**BOARD DIVERSITY: Any other Comments or suggestions** \_\_\_\_\_

<b>III BOARD SUB-COMMITTEES:</b> Below are listed some characteristics that describe Board Sub-committee. How would you rate the Board sub committees on each of the following?	<b>1</b> <b>Strongly disagree</b>	<b>2</b> <b>Disagree</b>	<b>3</b> <b>Neutral</b>	<b>4</b> <b>Agree</b>	<b>5</b> <b>Strongly agree</b>
3.1 The bank board room has established audit subcommittee, risk management and compliance sub-committee and human resource affairs sub-committee.					
3.2 The establishment of board subcommittees has played significant role and improved the bank corporate governance as the main board delegate specific tasks to the board subcommittee and utilizing the contribution of non-executive directors.					
	<b>1</b> <b>Strongly disagree</b>	<b>2</b> <b>Disagree</b>	<b>3</b> <b>Neutral</b>	<b>4</b> <b>Agree</b>	<b>5</b> <b>Strongly agree</b>
3.3 The Audit Sub-Committee provides independent oversight of the bank's financial reporting and internal control system and ensure checks and balances within the bank.					
3.4 The Risk Management and Compliance Sub-Committee oversees senior management's activities in managing credit, market, liquidity, operational, legal and other risk and ensure that the risk management process is in place and functioning.					
3.5 The Human Resource Affairs Sub-Committee provides formal and transparent proposal on the employment and removal of senior management members if they are ineffective, errant or negligent in discharging their responsibilities and on the overall compensation/benefit system of the bank.					
3.6 As one of the board of directors, you believe that the effectiveness of the board is influenced by board committees as the regulatory recommendations and the complexity of bank activities place emphasis on the importance of board committees.					
3.7 The bank board uses the above-board sub-committee structures to facilitate, evaluate, and ratify long-term investment decisions and to monitor the performance of senior management.					
3.8 As one of the board of directors, you believe that the different board sub-committees of the existing board room has a positive and significant impact on the bank Financial Performance(ROA).					

**BOARD SUB-COMMITTEES: Any other comments and suggestions.**

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<b>IV. BOARD MEMBERS EDUCATIONAL QUALIFICATIONS</b> Below are listed some characteristics that describe Board members educational qualifications. How would you rate the Board members educational qualifications on each of the following?	<b>1</b> <b>Strongly disagree</b>	<b>2</b> <b>Disagree</b>	<b>3</b> <b>Neutral</b>	<b>4</b> <b>Agree</b>	<b>5</b> <b>Strongly agree</b>
4.1 The bank board comprise of directors who as a group provide a mixture of core competencies such as banking, finance, accounting, management, economics, legal, business administration, auditing information technology and investment management.					
4.2 The bank board room has directors with higher educational qualifications and contributed for the board room to be innovative, creative, and better in strategic decision-making.					
4.3 The existence of qualified directors in the bank board room has increased the bank performance as they promote corporate image and demonstrate accountability and credibility within the team.					
4.4 The bank board room plays an important role in formulating and implementing business strategy as it is composed of directors who bringing expertise and knowledge.					
4.5 As one of the board directors, you emphasize on the board of directors' qualification rather experience for the bank existing and future business success.					
4.6 The bank bord has directors with varied skills that can assess the internal business conditions and scan the external environment properly in running the bank business successfully.					
4.7 As one of the bank board, you believe that the educational qualification of the existing board room has a positive and significant impact on the bank Financial Performance(ROA).					

**BOARD MEMBERS EDUCATIONAL QUALIFICATIONS: Any other Comments or suggestions.**\_\_\_\_\_

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<b>V NUMBER OF BOARD MEETINGS:</b> Below are listed some characteristics that describe Board meetings. How would you rate the Board on each of the following?	<b>1 Strongly disagree</b>	<b>2 Disagree</b>	<b>3 Neutral</b>	<b>4 Agree</b>	<b>5 Strongly Agree</b>
5.1 The intensity of board activity is measured by the frequency of board meetings as it indicates an active monitoring role of the board.					
5.2 The bank board meetings provide useful information in a timely manner which is critical for the board’s effectiveness.					
5.3 Board meeting time is adequate and has significant contribution for improving the effectiveness of the bank board.					
5.4 The more frequent of the bank board meetings provide board members with the chance to come together, and to discuss and exchange ideas on how they wish to monitor managers and bank strategy.					
5.5 The bank board members are meeting more frequently beyond their regular schedule meeting and it has contributed more to improve board performance and tends to generate higher for the bank financial performance(ROA).					
5.6 The board of directors believe that increasing the level of board activity through board meetings lead to better bank achievement and financial performance.					
5.7 As one of the board directors, you believe that frequent board meetings is not necessarily and useful because of the shortage in time for directors to exchange meaningful ideas among themselves.					
5.8 Member of the bank board aware and know that a director should attend in person at least 75% of the board meetings of a bank within the financial year.					

		1	2	3	4	5
		Strongly disagree	Disagree	Neutral	Agree	Strongly agree
5.9	The current practice of the board meetings is to 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 board meetings.					
5.10	The board member has showed their interest and brought their concern to the board table to increase the number of board meeting as it will have significant contribution for the bank financial performance(ROA).					
5.11	As one of the bank board directors, you believe that the frequent (increased) board meeting has a positive and significant impact on the bank Financial Performance(ROA).					

**NUMBER OF BOARD MEETINGS: Any other Comments and suggestions.** \_\_\_\_\_

<b>Vi BANK FINANCIAL PERFORMANCE (RETURN ON ASSET)</b>	1	2	3	4	5	
	Strongly disagree	Disagree	Neutral	Agree	Strongly Agree	
6.1	The bank had good improvement in its financial performance and the return on Assets has been improved during the last 5 years.					
6.2	The Corporate Governance practices of the bank board during the last five years has been improving and has significant contribution for the overall bank achievement and financial performance success specifically on Return on Asset (ROA).					
6.3	As a member of the board room, you believe that the Internal Corporate Governance mechanism of the existing board specifically the Board Size, Board diversity, Board sub-Committees, Directors Educational Qualification and the frequency Board Meeting have a positive and significant impact on the bank Return on Asset (ROA).					

**BANK FINANCIAL PERFORMANCE (RETURN ON ASSET): Any other Comments and suggestions.**

---

**VIII**

**GENERAL QUESTIONS**

1. Does your board have the following committees?      Yes      No
- (i) Audit Committee
- (ii) Nomination Committee
- (iii) Human resource affairs sub-committee \_\_\_\_\_
- (iv) Risk management and compliance sub-committee \_\_\_\_\_
2. Of the following, who has the strongest influence in the selection and dismissal of board of directors? (**You may choose more than one**)
- i. Board of directors \_\_\_\_\_
- ii. Audit sub committee \_\_\_\_\_
- iii. Human resource affairs sub-committee \_\_\_\_\_
- iv. Risk management and compliance sub-committee \_\_\_\_\_
- v. President/CEO-----
- vi. Others (please specify)
3. What is your view of corporate governance in your bank compared with other banks?
- Much better \_\_\_\_\_      Slightly better \_\_\_\_\_      About the same
- Slightly worse \_\_\_\_\_      Much worse \_
4. How do you compare your bank current corporate governance practices and financial performance with those of the previous years?
- Much better \_\_\_\_\_      Slightly better \_\_\_\_\_      About the same
- Slightly worse \_\_\_\_\_      Much worse \_
5. Which of the following Corporate Governance guidelines document/s the bank applies for the board operations and function? (**You may choose more than one**)
- (i) Relevant Commercial Code \_\_\_\_\_
- (ii) Requirements of the National Bank of Ethiopia (regulatory agency) \_
- (iii) Company Policy \_\_\_\_\_

(iv) Code of Corporate Governance \_\_\_\_\_

(v) Other, please specify

6. How often the bank board conduct meetings (frequency of meetings)?

Every two weeks

Every Month

Every three months

If different, please specify

7. What was your average attendance rate for board meetings per year?

90-100%

75-89% \_\_\_\_\_

60-74% \_\_\_\_\_

50-59% \_\_\_\_\_

Below 50%

8. What do you think of the current size of your board?

Too large

Too small

Ideal

9. If too large or too small, what do you think should be the ideal size of Zemen bank board?

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10. What are the major strengths of the bank Board?

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11. How could the Bord Governance be improved?

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12. Do you feel that Zemen Bank S.C is headed in the right direction? Provide rationale.

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13. In your opinion, what are the major Corporate Governance problems or issues faced by the bank?

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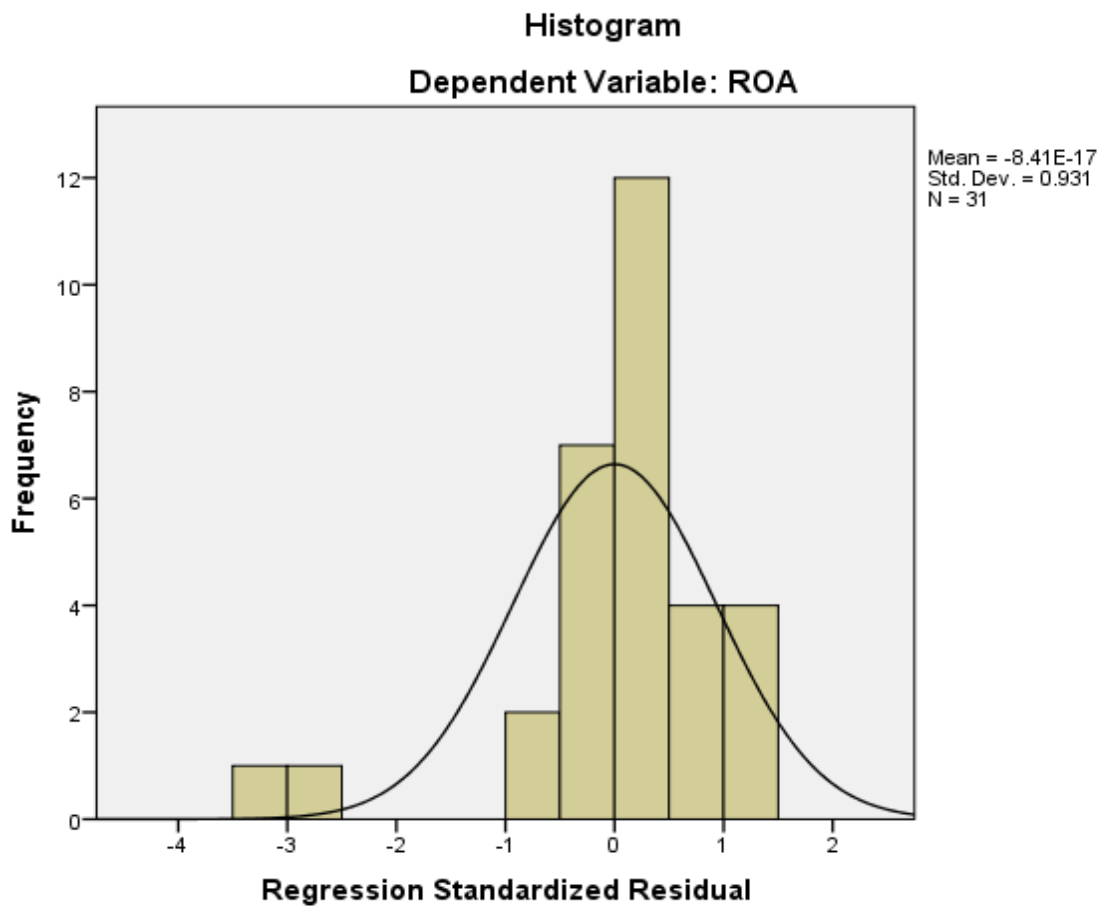
14. Any other comments?

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**END OF QUESTIONNAIRE**

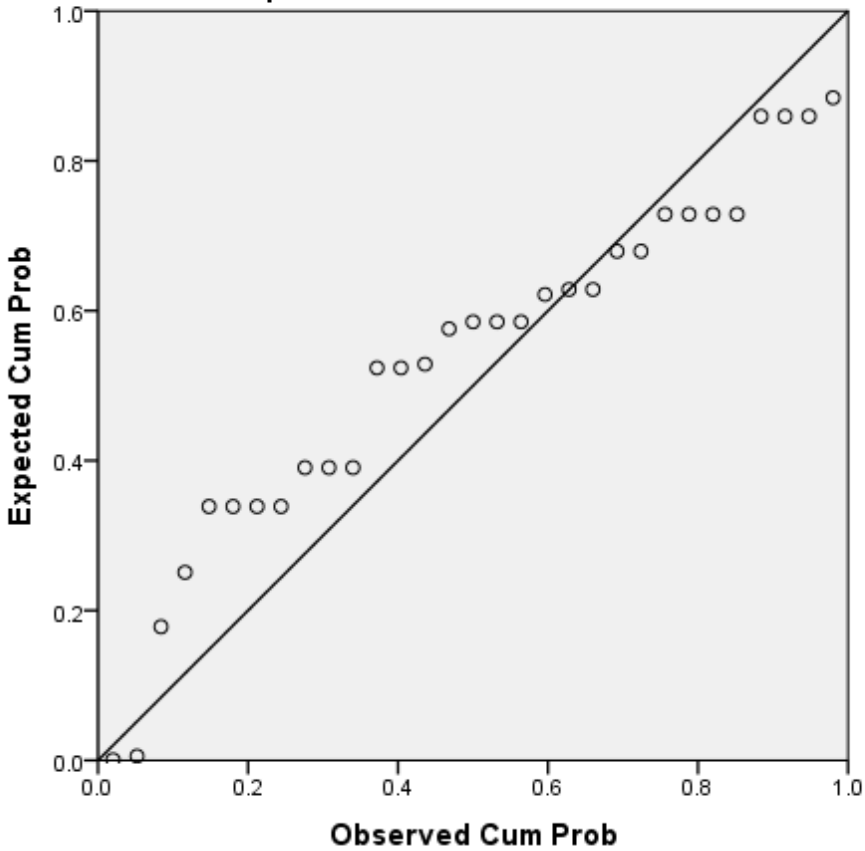
**Thank you very much for your participation.**

### ANNEX III: Normality test



Normal P-P Plot of Regression Standardized Residual

Dependent Variable: ROA



## ANNEX VI: SPSS Data Analysis Output

### Regression

Descriptive Statistics									
	N	Minimum	Maximum	Mean	Std. Deviation	Skewness		Kurtosis	
	Statistic	Statistic	Statistic	Statistic	Statistic	Statistic	Std. Error	Statistic	Std. Error
ROA	31	2.00	5.00	4.5161	.81121	-2.058	.421	2.376	.821
BS	31	4.00	5.00	4.2903	.46141	.672	.421	-1.134	.821
BD	31	3.00	5.00	4.3226	.59928	-.243	.421	-.537	.821
BSC	31	3.00	5.00	4.6774	.57079	-1.916	.421	2.161	.821
BMD	31	3.00	5.00	4.5806	.62044	-0.221	.421	.557	.821
NBM	31	4.00	5.00	4.3226	.47519	.798	.421	-1.462	.821
Valid N (listwise)	31								

### Correlation Test

Correlations						
		ROA	BS	BD	BSC	NBM
Pearson Correlation	ROA	1.000	.388	.400	.228	.159
	BS	.388	1.000	.132	.178	.319
	BD	.400	.132	1.000	.217	.442
	BSC	.228	.178	.217	1.000	.274
	NBM	.159	.319	.442	.274	1.000
Sig. (1-tailed)	ROA	.	.016	.013	.109	.196
	BS	.016	.	.239	.170	.040
	BD	.013	.239	.	.121	.006
	BSC	.109	.170	.121	.	.068
	NBM	.196	.040	.006	.068	.
N	ROA	31	31	31	31	31
	BS	31	31	31	31	31
	BD	31	31	31	31	31
	BSC	31	31	31	31	31
	NBM	31	31	31	31	31

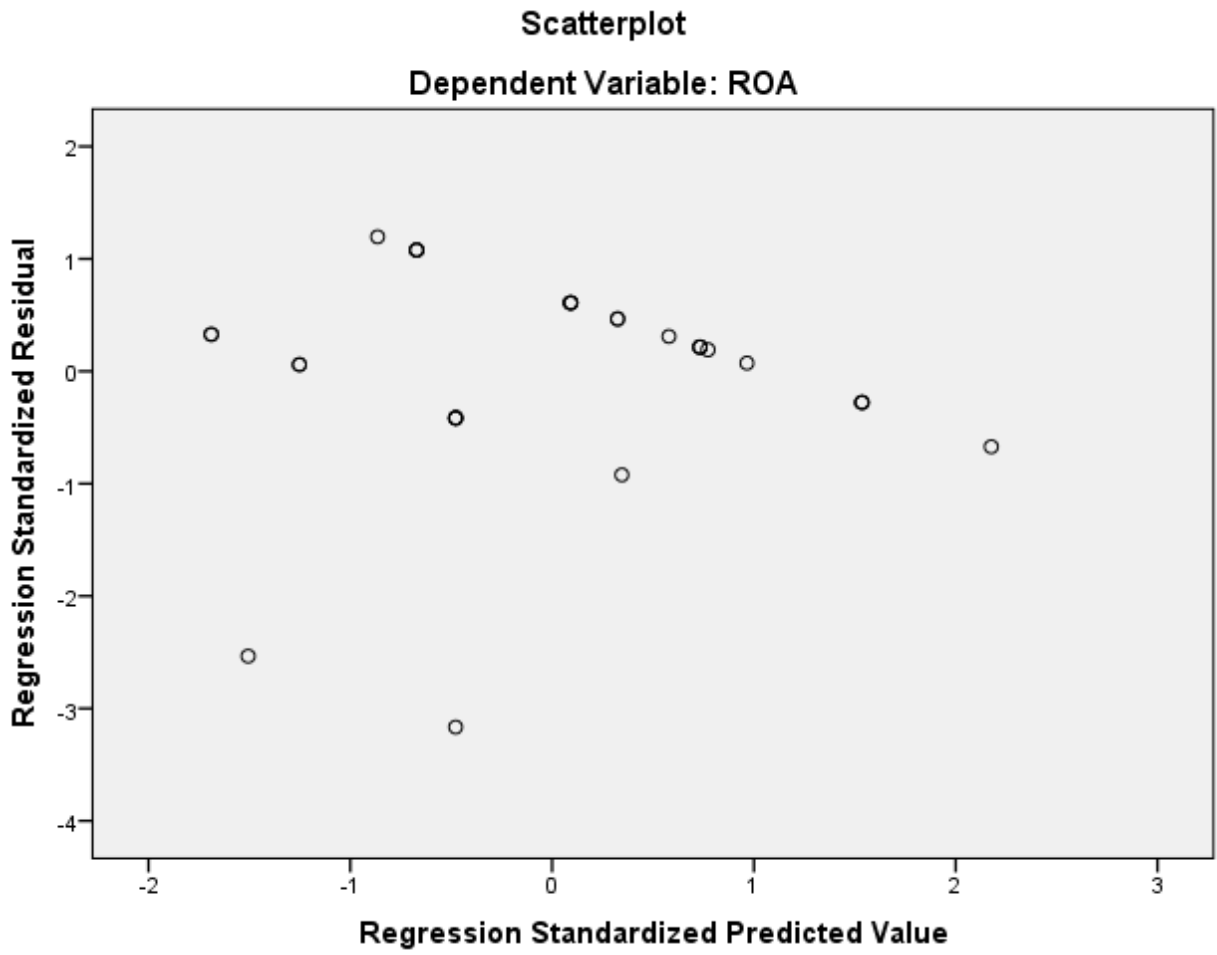
Coefficient Correlations <sup>a</sup>						
Model			NBM	BSC	BS	BD
1	Correlations	NBM	1.000	-.167	-.270	-.398
		BSC	-.167	1.000	-.101	-.113
		BS	-.270	-.101	1.000	.021
		BD	-.398	-.113	.021	1.000
	Covariances	NBM	.109	-.014	-.027	-.033
		BSC	-.014	.060	-.008	-.007
		BS	-.027	-.008	.093	.002
		BD	-.033	-.007	.002	.062

a. Dependent Variable: ROA

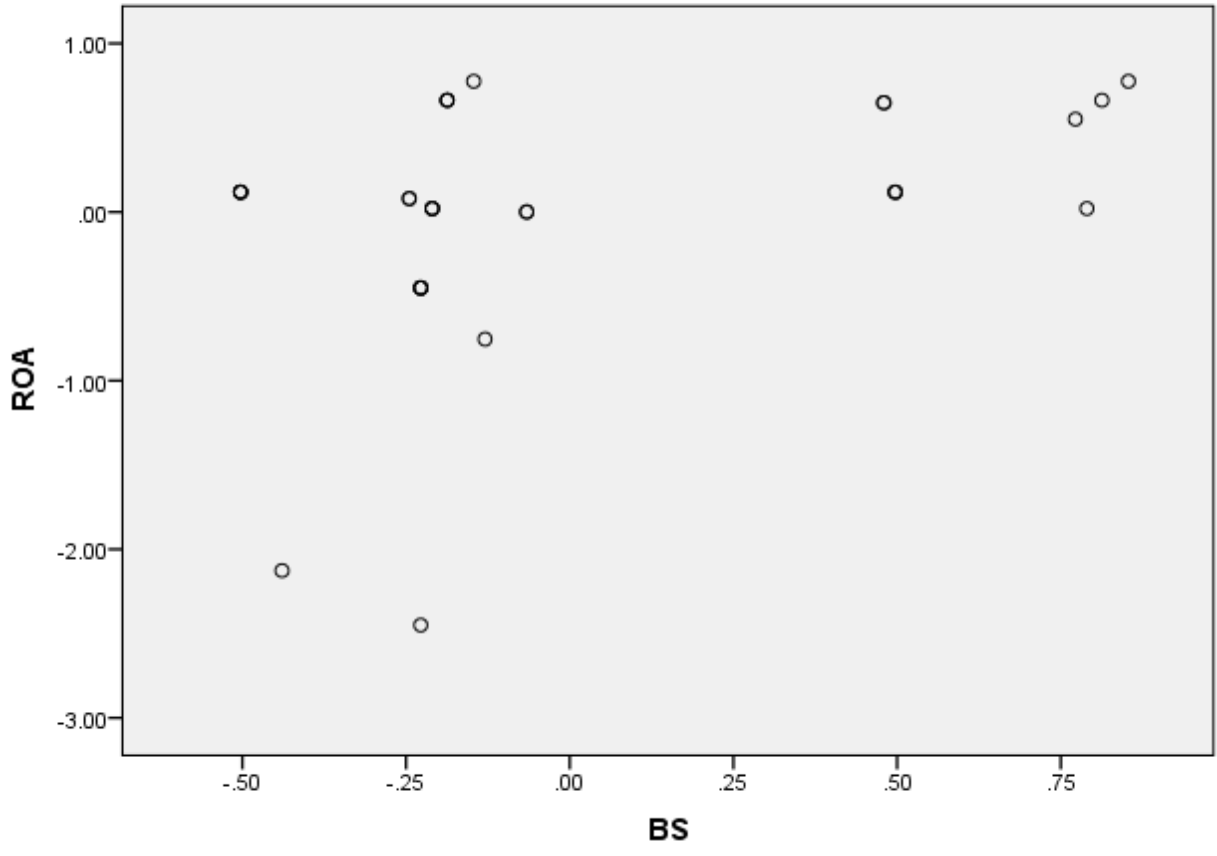
### Collinearity Test

Collinearity Diagnostics <sup>a</sup>								
Model	Dimension	Eigenvalue	Condition Index	Variance Proportions				
				(Constant)	BS	BD	BSC	NBM
1	1	4.964	1.000	.00	.00	.00	.00	.00
	2	.014	18.892	.01	.11	.70	.12	.01
	3	.011	21.478	.01	.30	.01	.74	.03
	4	.007	27.626	.01	.21	.26	.00	.93
	5	.004	33.247	.97	.37	.04	.14	.03

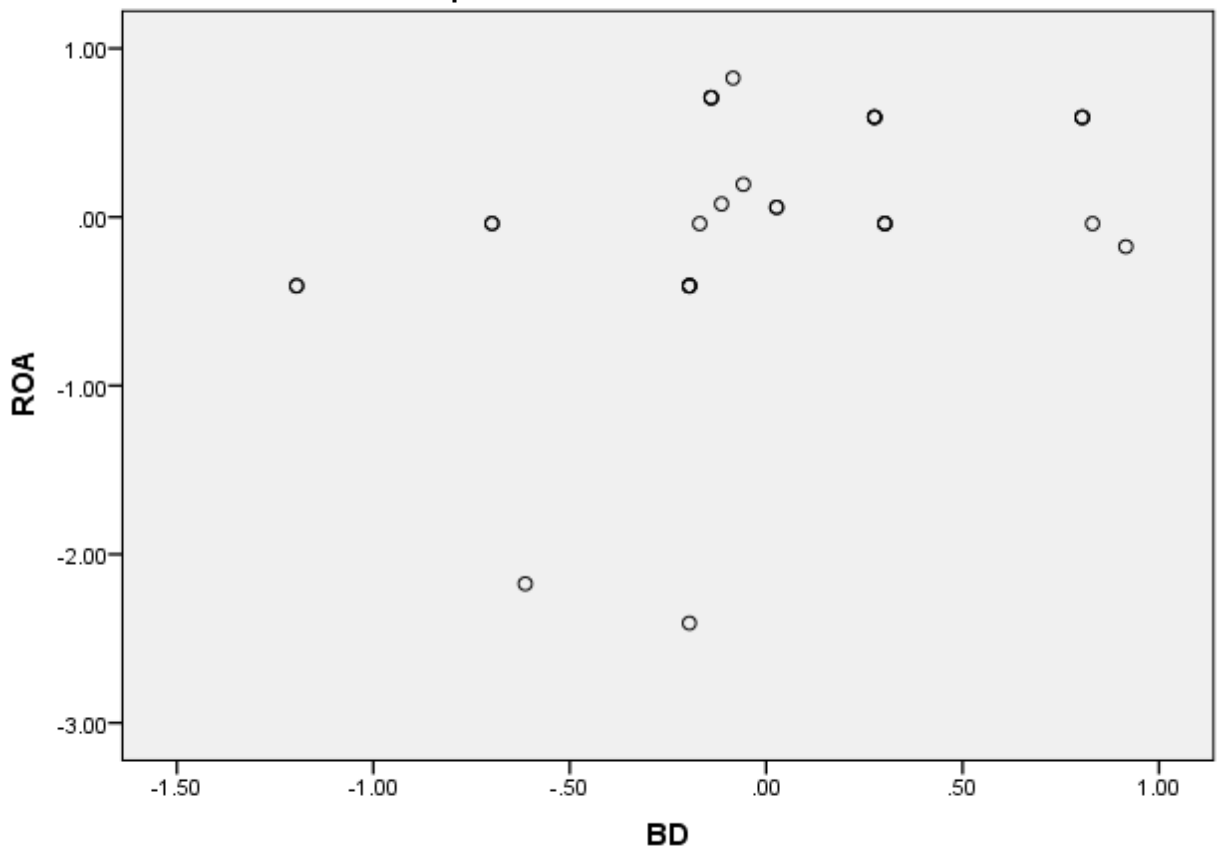
a. Dependent Variable: ROA



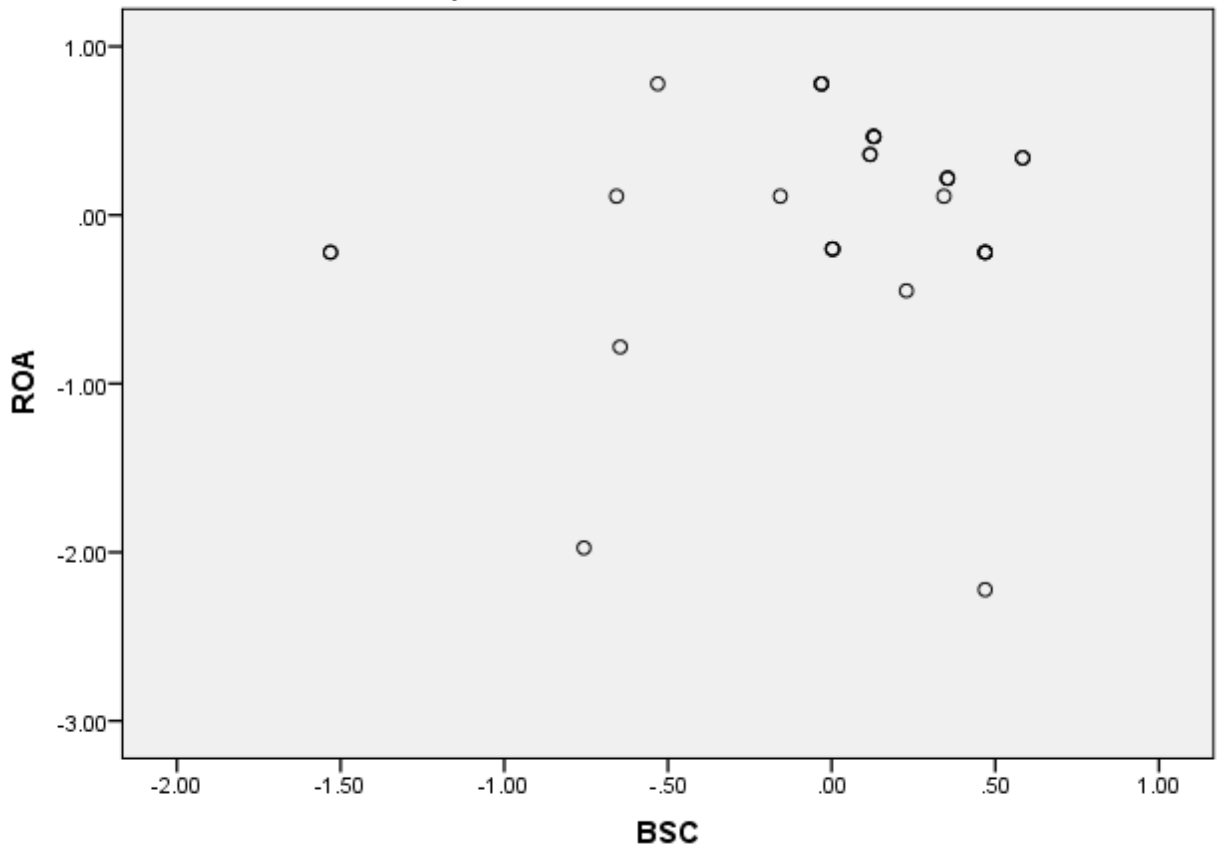
Partial Regression Plot  
Dependent Variable: ROA



Partial Regression Plot  
Dependent Variable: ROA



Partial Regression Plot  
Dependent Variable: ROA



Partial Regression Plot  
Dependent Variable: ROA

