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Essays on Corporate Governance and Firm Performance

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Received: 15th April 2021
Review: 19th Oct. 2021
Accepted: 16th Feb. 2022

Abstract

Purpose: The purpose of the study is to check how Corporate Governance practices by firms are increasingly becoming a critical element of a firm's performance and an area of great concern to all stakeholders, particularly market regulators and shareholders.

Design/methodology/approach: The current work approach to conducting a review of all relevant research issues around corporate governance. Researchers have developed various indices to measure Corporate Governance by using proxies like Board size, number of independent directors, the attendance record of board members, etc. Corporate governance practices are an important tool for reducing agency costs and an effective board, a higher proportion of independent directors, a vigilant audit committee, etc.

Findings: The studies have proved that corporate governance practices are more developed and associated with developed economic markets as compared to developing economies. Similarly, studies have evidenced that Corporate Governance systems and architectures are more observed in large firms whereas it is poor in small firms. Also, we highlight research work that clearly proves that Corporate Governance is better in professionally managed companies as compared to family own businesses. The current work also highlights the uniqueness of corporate governance in the banking sector.

Originality: The study is quite different from the other studies done related to Corporate Governance in the market as it is an overall summary to compare the level of Corporate Governance and its impact on the market performance by comparing the corporate governance in developed and developing economies, size of the firm, ownership structure and the special case for the banking sector.

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NMIMS Management Review
ISSN: 0971-1023
Volume XXX
Issue-3 | April 2022

https://doi.org/10.53908/NMMR.300212

Practical Implications: The work sends a very strong message to the markets (both the AMCs as well as the retail investor community) to watch out for corporate governance practices while making investment choices or decisions. Firms with a poor track record of corporate governance can be avoided while creating a portfolio and regulators need to keep a strict vigil on such firms.

Keywords: *Corporate Governance, Agency Theory, Agency cost, Board of Directors, Developed and Developing economies, Firm size, ownership, Firm Performance, Auditor Quality, Banks.*

Introduction

In the classical firm structure, the shareholder (the principal) is the one who invests their capital in a firm and their capital is managed by the manager (who is the agent). The agent must remember that whatever investment decisions they take regarding the investment of the capital (provided by the principal), the interest of the principal should be their first priority. (Jensen and Meckling, 1976) investigated the agency problem in corporate governance by developing theoretical frameworks for analyzing agency costs. Managers may become complacent and increase their risk appetite to boost their performance because they know that any loss will not put any impact on their personal wealth. The resulting miscommunication and disagreement may result in various problems and discord within the company. This contradiction between an agent and the shareholder becomes a cause for inefficiencies and financial losses. This leads to the principal-agentproblem. Companies should seek to minimize these situations through a well-defined corporate governance policy. The (Cadbury report, 1992) states that Corporate Governance is the system by which firms are directed and controlled. (Blair, 1995)refers to Corporate Governance as the set of legal, cultural, and institutional arrangements that determine what public corporations can do, who controls them, how that control is exercised, and how the risk and return undertaken are allocated.

1.1 Agency Cost and Role of the Board of Directors

Agency cost is a kind of internal cost that arises due to the actions of an agent on behalf of a principal, and it should be paid to the agent. Conflict of interest between management (agent) and the shareholder (principal) is the basic reason behind agency cost. The interest of the shareholder is to run a company in a way to maximizes the value for shareholders. Agency cost was first mentioned by (Berle and Means, 1932) who argue that when there is a separation between management and ownership in a company, the manager who acts as the agent of the company will be motivated and have the opportunity to conduct activities that serve their own interest instead of maximizing the value of the owners' wealth and power of management is not included in the interests of shareholders. (Jensen and Meckling, 1976) who defined the concept of agency cost shows the issue of separation and control. According to (Myers, 1997) the agency cost of debt are the increasing functions of growth opportunities available to the firm. There are two types of agency costs present in an organization: First, arising due to conflicts between the shareholder and the management, and the other one – due to conflicts between shareholders and debt holders (La Porta, Lopez-deSilanes, Shleifer and Vishny, 2002). (Ang et al., 2000) who measures the agency cost by the ratio of operating expenses to annual sales and by the ratio of annual sales to total assets. In addition, according to (Yermack, 2006) Free Cash Flow (FCF) is also a form of agency cost which increases the agency cost because managers use this approach for their own compensations and benefits. As a result, agency cost has a major impact on a few organizational decisions such as capital structure decisions, dividend policy decisions, etc.

The board acts as a governing body that typically meets at regular intervals to set policies for corporate management. The board is generally believed to govern the firm on the behalf of shareholders' interest. The Board of Directors plays an eminent role to make sure that an outward-looking approach such as transparency, integrity, and win-win relationship is valued within a firm and that these values are flourished at the firm-wide perspective. According to (Grove and Clouse, 2017) Boards are the organ in any organization selected by the shareholder to secure resource utilization and other benefits of shareholders and control the actions of the manager. The power has been given to the board in order to control the conflicts between the investor and the manager. The Board of directors acts as an important source to bridge the gap between the management and the shareholder.

The *paper is divided into 9 sections as follows:*

Section 1 is an Introduction. Section 2 talks about Corporate Governance (CG henceforth) Definition and Measurement of C.G. Section 3 determines CG practices in Developed Vs developing markets, Section 4 discusses CG and the size of the firm. Section 5 elaborates literature around CG issues in Family-owned businesses Vs Professional held companies. Section 6 talks about the linkages between CG and Firm performance. Section 7 talks about Auditor Quality, CG, and firm performance, and Section 8 mentions issues around CG in the Banking sector. Finally, Section 9 states future research agendas.

2. Corporate Governance: Definition

Corporate governance is defined as a set of rules, procedures, and practices by which firms are controlled and regulated. The governance structure identified the distribution of rights and responsibilities among the different participants such as shareholders, board of directors, managers, creditors, and other stakeholders. C.G includes procedures through which corporations' objectives are followed in the context of regulatory, social, and market environments. Organization for Economic Co-operation and Development (2004), defines Corporate Governance as the set of relationships between the shareholder, manager, stakeholders, board of directors, the employees. According to (The Cadbury Report, 1992) Corporate Governance acts as a mechanism to control and direct the functioning of the firm and create the balance among the shareholder, manager, and stakeholders. As per (Solomon, 2007) C.G. is the concept where the firm ensures transparency, social responsibility, and legal rights of stakeholders. According to (The Financial Times, 1997) corporate governance is the relationship of the enterprise to shareholders or in the wider sense the relationship of the enterprise to society as a whole. Corporate Governance is considered to be prominent in maximizing the owner's wealth and enhancing the firm performance through strategic policies. (Millstein, 1998) gives a narrow and broader definition of C.G. The narrow definition emphasizes C.G as the relationship between managers, directors, and shareholders that encompasses the relationship of the corporation to stakeholders and society. Whereas in her broader definition she defines C.G as the combination of laws, regulations, listing rules, and voluntary private-sector practices that enable the corporation to attract capital, perform efficiently, generate profit and meet both the expectations of society as well as the legal obligations.

2.1 Measurement of Corporate Governance

The issue of C.G and financial performance has always been a crucial and essential element of the firms. Good C.G practices are important in reducing the risk for investors and improving performance. An effective board of directors is one of the various mechanisms firms use in resolving agency conflicts between managers and shareholders (Fama and Jensen, 1983). Research on the role of the board of directors has focused on board effectiveness in monitoring management, where the degree of effectiveness has been associated with board independence. One measure commonly used to examine board independence is the percentage of outside directors on the board, where outside directors are individuals who do not hold an officer position in the firm. It is argued that the monitoring by outside directors reduces managers' discretion, and as a result lowers the agency costs (Bathala and Rao, 1995).

In this context, board independence and the associated monitoring are expected to have a beneficial impact on the firm's risk profile, and valuation. There are also numerous studies that have studied the relationship between board composition and firm performance, but the evidence is mixed. (Hermalin and Weisbach, 1991) find no relation between the percentage of outside directors and the general level of firm performance as measured by Tobin's Q. Three board attributes (board independence, board meetings, board attendance, board size, background of the independent directors, and board gender) were used as proxies of the independent variables while ROA was chosen as a measure of performance. The results obtained indicated that the relationship between board independence and ROA is negatively insignificant. By doing the comparison it was found that Board meetings and ROA were negatively significant. However, the association between board genders, board attendance, the board size, and ROA were negatively insignificant. It was observed that the relationship between firm size and ROA is positively significant. In correspondence to the same, the relation between bank age and ROA was found as negatively significant.

3. Corporate Governance in Developing Vs Developed Economies/ Markets

H1: Corporate Governance is better in developed economies in comparison to developing economies.

In developing economies like India, it has been observed that the per capita income is low in comparison to developed economies because of which there are fewer investors in the stock markets who want to invest their money to make profits by taking small risks. The investors believe that their money is not safe in the stock market, so they keep their money safe and secure in the banks (financial institutions) as Term Deposits, popularly known as Fixed Deposits. They consider it as the best tool for making investments which shows that they have a lack of social security and almost zero risk appetite, which satisfies them by gaining considerably low growth than the actual growth which the market can generate.

(Gurley and Shaw, 1955) enumerates that financial development is a positive function of real income and wealth. As the people in the developing economies are not very rich so they dither to take a risk and avoid any investment in the stock market. They find other investments like Fixed deposits, term plans, Recurring deposits, and investing in commodities like gold as the best way of keeping their money safe and secure and believe that they will not lose their money with such investments. This shows that investors in the developing economies manage their money in a traditional way and agitate to adopt the modern way of investment. They always have a fear that if they invest in the stock market they will lose their money as the information shared in the developing market is not adequate which breaks the trust of the investors.

This is a reality and even the firms willing to raise external funds also know that there is a very poor appetite for risky financial instruments. (Hartelius, Kashiwase and Kodres 2008) estimate a panel data model in which developing market spreads are a function of liquidity risk and fundamental factors. There are a few firms that generate regular growth and provide regular dividends and interest payments to their bondholders and shareholders. Developing countries are typically characterized by a large number of small, unproductive firms and very few large, highly efficient, and disruptive companies which emphasize less involvement of firms in the stock market as they cannot generate more revenue. Most of the firms in developing countries are able to conceal price-sensitive information from the markets, which again makes the investor's sentiments poor regarding the primary and secondary markets. Because of this the investors avoid doing any such investments which will make them lose their money.

If we look at historical records of different firms in the developing market, we can easily analyze that their records are not stable, and numerous corporate actions and information are leaked in history, which basically reduces trust. For example, initially, X firms start off with launching an IPO at an offer price of 500 per share, and soon after listing, the stock is trading at a price below the offer price. Such incidents, which contribute to significant loss to the investors, create fear in the mind of investors (general opinion) and thus people hesitate to make such investments in the capital market. (Young et al., 2008) states that policies designed for developed markets proved to be unproductive in developing economies.

On the contrary, if we talk about the developed countries, in terms of their economy, capital markets, and per capita income, most of these countries are high-income rich economies, so there will be more investors who will invest their money in the stock market to generate more profit. In developed countries, investors take a high risk to get good returns as they have the right information about the market and its situation. The firms in the developed markets are more organized and have systematic corporate management practices and processes when compared to emerging markets firms (slightly less regulated). According to (Lins, Strickland, and Zenner 2005), developed markets enhance access to the external capital market by showing the sensitivity of investment to cash flow in comparison to emerging economies. Most of firms reveal price-sensitive and authentic information on time, which develops confidence in the investors, and they do not hesitate to invest. The competitive forces in the developed economies are stronger which makes the firms more competitive and this will enhance the firm performance as all the firms will try to excel themselves in terms of the right information and more revenue. The information shared by the firms in the developed economies is genuine which will make the investors make their investment in the stock market, also this will develop confidence in the investors and they feel safe and secure while doing such investments. The Judicial and the overall institutional system in the developed market is very strict and stringent with a lot of powers, strict action is taken towards the wrong information or any misconduct performed in the market, whereas in the developing countries the judicial system is not very effective. The basic elements such as reasonable time to disposition; and inadequate court-provide remedies are missing in the developing countries. (Sherwood, 1995) states that judicial reform will significantly improve economic performance.

Generally, in developing countries, the judicial system does not come close to the goals of the judiciary, which should be capable of applying and enforcing laws equitably and efficiently, and laws often are not subject to predictable interpretation. (Walker and William 1995) the *U.S. Agency for International Development (USAID)* funds judicial reform as part of its larger effort to strengthen newly emerging democracies around the globe.

Small or start-up businesses are affected by the lack of access to a predictably impartial and efficient judicial system which creates uncertainties that hamper the completion of new transactions. (Pistor, et al., 1999) reviewed the judicial and economic reform in transition economies and discovered that the factors that contribute to economic reform and development may also be responsible for improvements in the judiciary. According to (Ellickson, 1997) judicial and economic reform is a result of preexisting attitudes and beliefs in society at large, or what has recently been termed "social capital."

Conclusion: *Result accepted, as there are more studies done in developed economies that define better corporate governance in comparison to developing economies.*

4. Corporate Governance and Size of the Firms

H2: Corporate Governance is better in Large Firms in comparison to small firms

Good corporate governance is not when a business makes a 'right' decision. Rather, it is when a business ensures that there is a good decision-making process in place. (Gregory, 2000), emphasis good corporate governance as the ability to find funds from financial markets, being able to operate efficiently parallel to corporate establishment objectives, meeting stakeholder expectations, complying with the laws of the countries. A large business definitely is more complex in terms of its processes and decision-making hierarchy can be really long and interlinked between various functional and geographical areas, but till the time the "Process" of decision making is meticulously laid down and strictly followed, the size of the firm shouldn't really matter. Large scale firms all start their operations as SMEs, but they become large by completing many difficult cycles (Özgener, 2003). (Akin, 2002) states an entrepreneur (SME) encounters many difficulties, especially in the growth cycle, in each cycle. A small business may have a fairly small auditor, a simple governance structure, a smaller board of directors, and simple processes for decision making so that small businesses can also ensure they have good governance in place. (Cochran, 1981) define a small business as total net worth, relative size within the industry, number of employees, the value of products, and annual sales or receipts. But when we look at the reality on the ground, small firms struggle to fulfill sound corporate governance policies and principles. The reasons could range from family ownership of the business to a lack of resources to hire better auditors, independent directors, or simply the sheer lack of incentive to be more transparent in decision making.

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NMIMS
Management Review
ISSN: 0971-1023
Volume XXX
Issue-3 | April 2022

- **Need for External funding is almost nil in small firms.**

As the small firms are basically family-owned businesses so they do not need external funding in the form of loans or equity. They set their own goals, policies, and procedures to have a good corporate governance structure. Small firms are required to adjust in areas such as information and transparency, innovation, performance and risk evaluation, and auditing. According to (Beck and Demirguc, 2006) there is substantial evidence that small firms have less access to formal sources of external finance.

- **Mostly Family-owned businesses: major shares held by family members**.

If we compare small businesses with large businesses, we can analyze that the major shares held in small firms are by the family member whereas in large firms' major shares are held by the institutional shareholders who get the right to have control over the firm. In small firms the control is in the hands of family people, there will be no interference from the external investors so they will create their own strategy of dealing with the things in the organization. In the USA family businesses represent 35% of all businesses, in Europe over 50% (Faccio and Lang, 2002) and in Asia over two-thirds of businesses (Claussens et al., 2002).

- **Large firms need external funding, either through bank or equity markets.**

In both situations, transparency in decision-making and well-laid down governance architecture is a prerequisite. Large firms are funded externally in the form of loans and equity shares, there are institutional shareholders who hold some shares in the firm. If any institutional shareholder has 2-5% of shares in the firm then they will have the right to sit in the board meetings, they will be involved while making any decision. The processes and practices performed by the large firms are systematic and organized, which makes the firms operate significantly in a better way in comparison to small firms. As stated by (Durnev and Kim, 2005) highly profitable firms are seen to adopt good corporate governance frameworks. This is because such firms utilize more internal resources and less outside financial resources.

- **Small firms can't hire/don't need costly big auditors**

Most small business owners don't hire auditors for their firms as they believe that their money can be managed alone. Audits are really, really expensive, that is why savvy small companies that are not required to have an audit often opt for a 'review' of their financial statements instead. A review is an overall scope and the level of assurance that the audit firm provides, but it is a far bigger step down in terms of cost. If small businesses expand to medium size businesses, then they hire small auditors who can validate the financial report of the firm. (Eilifsen et al., 2001)state that management establishes and maintains both internal and external control mechanisms to provide assurance regarding the integrity of financial information for themselves as well as external parties. (Jensen and Payne, 2003) state regardless of the size of the business, managers value the integrity of financial information, because accurate financial information helps them make better decisions.

- Small firms can't hire/don't need costly independent directors in their Board as the fund allocated to the business is quite low and they cannot bear the expenses of independent directors. Also, they don't have institutional shareholders who can act as an independent director if required.
- Since small firms are not listed in stock markets, investment banks and broking/equity research houses don't follow them extensively.

Conclusion: *Mixed Result which states both large and small firms maintain a corporate governance system at their level.*

5. Corporate Governance and Ownership Structure (Family held business vs Retail Vs Institutional)

H3: Corporate Governance is better in Institutional ownership in comparison to Family owned and Retail ownership.

Businesses not only rely on the size and industry but also on their own. Some are owned by one person or a small group of people, some are owned by a large number of shareholders, some are owned by charitable foundations or trusts, and some are even owned by the state. Different ownership overlaps with different strategies of working, with different policies and legal forms that a business can take. (Jensen and Meckling, 1976) states ownership structure in terms of capital contributions. Corporate Governance is the system of rules, practices, and processes by which a firm is controlled and directed; it differs with the different ownership. It can be highlighted through family-owned, retail ownership, and Institutional ownership. According to (Zheka, 2005) ownership structure is constructed by using variables that include a proportion of foreign share ownership, managerial ownership percentage, largest institutional shareholder ownership, largest individual ownership, and government share ownership.

According to (Casrud et al., 2014) family business is defined as a business in which ownership and decisions are made by a group of family members." (Intihar and Pollack, 2012) state a family business refers to a business that is owned and managed by a family. The family-owned businesses are basically controlled and regulated by family members. The rules, regulations, and procedures are mostly governed by the family members who generally control the whole system. 70 % of businesses in most countries are family-owned businesses and thus play a key role in economic growth and workforce employment.

Most of the businesses in the countries are families owned which are operating at a small level and are also not registered in the stock market. The businesses expand from small to medium-sized then conglomerate to large-sized businesses. Brands such as Wal - Mart, Nike, BMW, Reliance, etc. have reached a peak of success in their respective businesses and had all started as family-owned businesses. As per Pearl Initiative & Price water house (Coopers, 2012), it has been observed that several large multinational corporations started their businesses as Family Businesses, and around 90% of the world's businesses are Family Businesses, in developed, developing as well as emerging markets with the majority are small and medium-sized enterprises (SMEs), but few are very large companies. The business has been able to achieve huge success with their successive generations over the years that have knowingly or unknowingly adhered to principles and requirements of corporate governance. A study by (CII, 2001) states that 75% of employment, 65% of GDP, and 71% of market capitalization in India is contributed by Family businesses. Only 38 % of Family Businesses in India survive after the 1st generation, 12% after the second generation, and only 3% after the 3rd generation. Of those that do last, 88% either deteriorate or fall apart before the fourth generation takes the reins. All the important decisions at the initial stage of the business are taken by the founder or his/her immediate offspring. The decision is a selfless decision taken for the overall benefits of the business. With time when the business grows more and more family members get associated with the business and gradually it leads to a stage of conflict of interests amongst the family members which becomes harmful for any business. So, in order to have control over these corrective steps are taken by involving the implementation of corporate governance. Corporate governance signifies transparency in the system. Many studies have shown that dominant family shareholders are common in many countries, both developed (Faccio and Lang, 2002) and developing (Claessens et al., 2002).

If we talk about the Retail investors, they are the individual investors who make small investments in order to make a profit which adds to their salary. They basically consider company shares as the mode to raise their income. These investors are the non-professional people who buy and sell securities or funds that contain a basket of securities. They have their personal account through which they can buy and sell the shares. They are the passive shareholders who are not active and do not analyze the firm closed on a day-to-day basis, as their investment is not big.

Institutional shareholders are those who pool money to purchase assets in the form of securities, real property, and other investment assets or originate loans.

Institutional investors include banks, credit unions, insurance companies, pension funds, mutual funds, etc. (Shleifer and Vishny, 1997) examines that in many regions of the world, corporations often have large shareholders playing active roles in corporate governance. (Velury and Jenkins, 2006) states institutional investors have an influence on firms because of their substantial shareholdings, and they can monitor managers. The research elaborates that the presence of institutional investors can change a firm's behavior through their monitoring activities. This is because (Arora and Sharma, 2016)state institutional investors are believed to have financial resources, skills, and experts that allow them to actively engage in monitoring activities compared to individual shareholders with limited resources. Their investment is big around 5-6% in any company; they can smartly analyze the numbers and are highly active investors. As their investment is high, they are more concerned about the company policies, rules, and procedures that they analyze on a day-to-day basis. Institutional shareholders play an eminent role in promoting good corporate governance. As the institutional investors represent large chunks of shareholders so they have proper control over the tendency and decision making (risk appetite) of the managerial class. On the other side, they can monitor the health of the firm because they have the necessary expertise and knowledge in running an organization since they sit on the boards of other companies as well. (Giannetti and Simonov, 2006) suggest that institutional investors prefer stocks of companies with a good governance structure.

These shareholders are more effective in comparison to minority or small investors, their statements or any suggestion cannot be overruled as it is done with the small investors because they do not have a large number of shares. Institutional shareholders usually don't pursue radical changes; instead, focus on maintaining the financing and operational efficiency of the organizations and promoting good Corporate Governance. (Hartzell and Starks, 2003) states that increased monitoring, measured by institutional ownership concentration, is associated with a higher fraction of a CEO's salary that is paid in equity.

Indian Firms mostly are family-owned businesses and therefore the quality of governance is always a question mark but with growing interests among the retail shareholders in terms of wider participation, sooner or later, they will also dilute their holdings and become more diversified in terms of ownership. Institutional shareholders bring in shareholder activism which is so important to keep a check on managers' decision-making as they may have a tendency to take risky decisions at the cost of the poor shareholders.

Conclusion: ***Accepted, Corporate Governance is a major concern in Institutional ownership in comparison to family-owned and Retail ownership***

6. Corporate Governance and Firm Performance

H4: Good Corporate Governance emphasizes good firm performance

C.G is the set of processes that provides an assurance to the investors of genuine return on the investments done by them in the firm. Corporate Governance involves the relationship among shareholders, other stockholders, management, board of directors, managers(agents)

(P.A. Gompers, L. Ishii, and A. Metrick, 2003) found a strong correlation between corporate governance and stock returns throughout 1990 and firm value, as measured by Tobin›s Q.(L.D. Brown and M.L. Caylor, 2004) examines that companies that are managed better would be more profitable, more valuable, and pay more cash dividends to shareholders.

In order to have effective Corporate Governance proper mechanism should be there through which the whole system is managed. The firm should respect the rights and interests of the shareholders, which can be possible with proper control on the activities of the managers as they manage the fund of the shareholders, companies that are managed better have better operational performance, the performance measures used by (Brown and Caylor, 2004). If it is not managed properly and the shareholders are not given proper information by the firm they cause conflicts between the agent and the shareholders which leads to agency costs. For which Board of directors is appointed by the firm. According to (Fama and Jensen,1983) board of directors is an internal control mechanism that is essential in monitoring top management. If the firm is unable to consider the problems of the shareholders and fails to make any committee that looks for the benefit of shareholders, then it creates poor governance which impacts the performance of the firm and leads to doubts in the mind of investors and they will hesitate to invest in such firms. (Shaheen and Nishat, 2005) relates corporate governance to the firm performance and analyses that firms with relatively poor governance are less profitable, less valuable, and pay out less cash to their shareholders. (Nandelstadh and Rosenberg, 2003) provide evidence that firms categorized by inefficient corporate governance have delivered inferior returns to shareholders while firms characterized by efficient corporate governance have been valued higher.

The firms which have good corporate governance tend to affect firm performance in two different ways: 1) Good Corporate Governance builds up confidence in the investors that their lesser amount of cash flow will be diverted and a higher proportion of the firm's profit will flow back to them in the form of return.

Second, good C.G reduces the expected return on equity which ultimately reduces the monitoring and auditing costs of shareholders. Good C.G is based on six important parameters such as Board of Directors independence, Board of director's diversity, Remuneration, CEO characteristics, Oversight, Ownership Structure. Using both accounting and market data for the year 2004 of 52 United Arab Emirates (Aljifri and Moustafa, 2007) provided evidence of the impact of corporate governance mechanisms on firms' performance.

Conclusion: ***Accepted, Firm that aims for good corporate governance always have good firm performance.***

7. Corporate Governance, Auditors Quality, and Firm Performance

H5: Firm performance is better where the auditor quality and corporate governance are good.

Corporate governance is the practice of directing, organizing and controlling the firm's decision-making at the strategic level. It is based on the principles of transparency, accountability, and fairness.

To maintain transparency and accountability in the system, the firms appoint an auditor who is authorized and certified personnel that reviews and verifies the accuracy of the financial statements and records of the firms. They inspect and examine the errors in the financial record and detect the reliability of the firm. An audit of financial statements has an extremely high degree of reliability and validity in comparison with unaudited firms. (Pownall and Schipper,1999) defined transparency as "the standards that reveal the events, occurrences, judgments, and estimates as to financial statements and their applications".

Large firms which are registered in the stock market choose Big 4 auditors like Deloitte, KPMG, PWC, and E&Y who take the responsibility to examine the financial statements of the firm which makes the firm more reliable and develops confidence in the investors. Good auditor ultimately leads to good corporate governance and may enhance the overall market performance of the firm. Also, they develop trust in the investors, and they will not hesitate while doing investments in the firm as they are assured of good auditor quality and good corporate governance. (Palmrose, 1986) suggest that the big-8 auditor's audit charge high fees because of high audit quality. (Martinez, and Moraes, 2014) found that auditors imposing higher audit fees will give a signal to markets that high audit quality may enhance shareholder value, the auditor quality plays an eminent role in the firm performance. There are a few things through which the auditor quality can be determined. According to (De Angelo, 1981) audit quality is the market assessment of the probability that first the auditor might discover the material misstatement in financial statements and or the accounting system of the audit client, and second that he will report the discovered material misstatement. The auditors who are more qualified and experienced will be preferred as they can examine more accurately and prepare correct reports in comparison to the auditors who are less qualified and experienced. The auditor should be experienced in the relevant field in which they are going for an inspection. If an auditor is going for the inspection or examination of an IT firm, he/she should be knowledgeable in the IT field and carry a few years of experience in the same, which makes the process more authentic and reliable. (Libby & Fredrick 1990) found that the more experienced the auditors are the greater is their understanding of misstatement in financial statements. Therefore, they have concluded that the quality of the auditor's decision improves as his auditing experience increases Auditor fees are another thing that impacts the quality of an auditor. The top auditors will have high fees that cannot be afforded by the small firms. In developing countries like India, most of the firms are small and family-owned so they cannot afford top-level auditors as they are very costly, so they generally choose medium and low-quality auditors who can audit the financial record of the firm which can make the firm's financial statements more reliable and valid. It has been believed (Simunic, 1980) that large audit firms invest a lot to increase their audit quality.

The auditor quality can be enhanced with the proper audit committee. The firms which have good corporate governance have a committee under which some of the board members are nominated and responsible for making decisions in the firm. (Krishnan and Schauer, 2000) evaluated the relationship between the firm size and audit quality and concluded that large audit firms have better service quality than small audit firms. In the same way, the audit committee is also responsible for recommending to the board regarding the appointment, re-appointment, and if required the removal of the statutory auditors and the fixation of audit fees. The audit committee is required to review with the management the annual financial statements before submission to the board for approval, especially with respect to changes in accounting policies and audit qualifications. (Teoh and Lim, 1996) investigated the effect of several factors including the audit committee of the audit client on the auditor independence.

Good audit quality always aims for good corporate governance which may play an important role in the enhancement of the firm performance. When the firm is audited in the right way, then it will be able to maintain transparency, accountability, and fairness in the system and develop a good image in the market.

Conclusion: ***Accepted, Auditor quality, and good Corporate Governance always aim for good firm performance***

8. Corporate Governance in Banks: Why are Banks "Special"?

When we consider Banks as firms then the structure is defined as such when both depositors and shareholders invest their money in Banks. In banks, the major concern is on the depositor's money as they save their money in banks only because they find it the best tool for savings in a developing economy like India. The investments made by the shareholders are less in comparison to depositors in banks. So, the major focus is on the depositor's money which is taken care of by the agents who utilize the money in creating loans. But this can cost the depositors as well shareholders as it's their money. Managers sometimes overlook the interest of the depositors as they are not afraid about any pros and cons.

The default risk is the oldest, most important, and primary risk in the banking sector as the main function of a bank is borrowing from their customers to give loans to others. In a country like India, most of the depositors or customers find banks as the safe zone for their money, and this money is utilized by the managers (agents) by giving loans which sometimes become default. This default in loan can have both short-term as well as long-term impacts. Under normal conditions, there is a probability of 2% to 5% default of the total number of loans disposed of. This would lead to weathering away the wealth of the shareholders (principals) who purchase shares of the bank; they take high risks in order to get a high return. When this probability of default increases from 5% to 20% of the total loans disposed then this would not only impact the shareholders (principals) wealth but also would have an effect on the depositor's money who keeps money in a bank as they find the bank as a secure place for their money-saving. They consider banks as a safe zone where their money can be secured. This shows the trust of the society in the bank as they find it best for social security. So, this impact of long-term default will create a major issue as it will keep the money of depositors at risk.

When the default is for the long-term then the depositors are affected, and the situation arises when the depositors are not able to get their own money which they saved in the bank with the assurance that their money is safe, and they are assured with some insurance amount. And sometimes the amount is paid by the government which actually uses the money of the taxpayers. This led to a critical phase that should be controlled, so in order to control this situation, the governance factor becomes very essential as it is very effective in building credibility, ensuring transparency and accountability as well as maintaining an effective channel of information disclosure that would foster good corporate governance. Under which the managers (agents) are being controlled and monitored by the Board of Directors so that they can be controlled from aggressive lending, which is done by the managers (agents) in order to raise the amount that causes to huge default in the system and creates Non-Performing Assets (NPA) which have an adverse impact on the banking system. Therefore, the lending should be done in a balanced way with proper authentication.

9. Agenda for Future Research

Most of the Corporate Governance studies are done in developed markets in collaboration with developing markets.

The Corporate Governance reports are qualitative, which is a time-consuming process.

There is continuing need to study corporate governance mechanisms and firm performance.

Also, there is a need to study the role of Corporate Governance and stakeholders in both public and private sectors.

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Issue-3 | April 2022

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