



# Economics and Business Quarterly Reviews

---

**Ma'aji, Muhammad M., Anderson, Ediri O., and Colon, Christine G. (2021), The Relevance of Good Corporate Governance Practices to Bank Performance. In: *Economics and Business Quarterly Reviews*, Vol.4, No.2, 35-46.**

ISSN 2775-9237

DOI: 10.31014/aior.1992.04.02.343

The online version of this article can be found at:  
<https://www.asianinstituteofresearch.org/>

---

Published by:  
The Asian Institute of Research

The *Journal of Economics and Business* is an Open Access publication. It may be read, copied, and distributed free of charge according to the conditions of the Creative Commons Attribution 4.0 International license.

The Asian Institute of Research *Journal of Economics and Business* is a peer-reviewed International Journal. The journal covers scholarly articles in the fields of Economics and Business, which includes, but not limited to, Business Economics (Micro and Macro), Finance, Management, Marketing, Business Law, Entrepreneurship, Behavioral and Health Economics, Government Taxation and Regulations, Financial Markets, International Economics, Investment, and Economic Development. As the journal is Open Access, it ensures high visibility and the increase of citations for all research articles published. The *Journal of Economics and Business* aims to facilitate scholarly work on recent theoretical and practical aspects of Economics and Business.



ASIAN INSTITUTE OF RESEARCH  
Connecting Scholars Worldwide



# The Relevance of Good Corporate Governance Practices to Bank Performance

Muhammad M. Ma'aji<sup>1</sup>, Ediri O. Anderson<sup>1</sup>, Christine G. Colon<sup>1</sup>

<sup>1</sup>CamEd Business School, Phnom Pehn, Cambodia

Correspondence: Muhammad M. Ma'aji, CamEd Business School, No. 64 Street 108, Phnom Penh Cambodia.  
Tel: +855 9625 96004. E-mail: muhammad@cam-ed.com

## Abstract

The purpose of this paper is to examine how corporate governance instruments impact firm value in the context of Cambodian banks. This paper considers foreign and domestic-owned banks in Cambodia. This study opts for a balanced sample of foreign and domestic owned banks for the period 2014-2018. Panel data regression is adopted for estimation of main results. The suitable model, i.e. fixed and random effect model is selected using the Hausman specification test where the result shows that the random effect model using generalized least square (GLS) regression is more suitable for the analysis. The findings show that Cambodian banks are having a substantially higher percentage of NEDs on their board, high implementation of governance procedures on board committees where on average the banks are having more than the required two board committees (audit and risk committees) as required by the Prakas on the governance of banks by National Bank of Cambodia. The average board size is around 8 members of which at least 3 members are having a postgraduate degree or a professional qualification. Policymakers need to improve on their supervisory function as the majority of the domestic and some foreign banks do not disclose their annual reports on their company website as required by the Prakas on Corporate Governance of Banks operating in Cambodia. Moreover, amendments should be made to the current corporate governance code for financial institutions as there are no explanatory notes that guide companies and therefore, the current guideline is open to individual and subjective interpretation.

**Keywords:** Board Size, Board Independence, Board Meetings, Corporate Governance

**JEL:** G30, G39

## Introduction

Cambodia has maintained strong economic growth over the last two decades, achieving on average 7 percent GDP growth. This remarkable achievement to some extent is linked to improving corporate governance practices among businesses in Cambodia especially the financial institutions leading to increase public confidence in the banking system among businesses, depositors, investors, business partners, and attracting more foreign direct investment (FDI) (Sokhorn, 2016). Financial institutions such as commercial banks are considered to be the engine growth

of economic development and sustainability of many countries as they give out credit to businesses and individuals that will stimulate economic activities (Berger, Klapper, Peria & Zaidi, 2008; Cheng & Degryse, 2010; Andrianova, Demetriades & Shortland, 2008). Commercial banks play a central role within the economy as they attract citizens' savings in the form of deposits, offer means of payment for goods and services, and finance the development of businesses. Banks are subject to stricter regulations in comparison with other entities because they are responsible for protecting the rights of the depositors, ensuring the stability of the payment system, and reducing unsystematic risk. Therefore, weak and ineffective corporate governance mechanisms in the banking sector can affect banks' performance and the economy as a whole (Allen, Qian & Qian, 2005; Zakaria et al., 2018). Hence, the implementation of strong governance practices in the sector is essential to have effective and robust bank systems and maintain a high level of public confidence in the system (BCBS, 2006; Burlaka, 2006; Gebba, 2015; Levine, 2013; Zakaria et al., 2018).

Good corporate governance practices make companies more accountable and transparent to their various stakeholders by balancing the interests of all stakeholders, including those to whom the company has legal, contractual, social, and market-driven obligations as well as to non-shareholder stakeholders, including employees, investors, creditors, suppliers, local communities, customers, and policymakers (Albrecht, 2016; Cheng & Degryse, 2010; Demetriades et al., 2008; OECD, 2015). Effective governance contributes to the development and increased access to capital by encourages new investments, boosts economic growth, and provides employment opportunities. For the banking sector specifically, improved corporate governance will boost the confidence of investors, reduces the risk of capital outflow from the economy, and at the same time, increases the flow of capital into the economy (Pagano & Volpin, 2004; Shleifer & Vishny, 1997; Stein & Daude, 2001; Talamo, 2009; Talamo, 2011). The degree of adherence to the basic principles of corporate governance by the banks at the corporate level enhances the confidence of shareholders and potential investors require access to regular and reliable information in detail for them to assess the management. Therefore, good corporate governance in the banking sector will help better manage risk, enhance internal control, and ensuring sustainable growth for the sector.

A considerable number of studies have been conducted before and after the global financial and banking crisis of 2007–2008 to enhance the understanding of bank governance and to assessed specific features of banks and their influence on the corporate governance mechanism (Gebba, 2015; Kirkpatrick, 2009; Laeven, 2013; Levine, 2004; Marcinkowska, 2012; Macey and O'Hara, 2003; Maxfield et al., 2018). However, most of the existing literature mainly seeks evidence from the developed countries. Therefore, there is still room for contribution to the literature on the effectiveness of corporate governance mechanisms in the banking sector with evidence from developing countries such as Cambodia. Furthermore, since the implementation of the corporate governance code for banks and other financial institution in 2008 namely "Prakas on Governance in Banks and Financial Institutions" (Corporate Governance Code on Banks) by the National Bank of Cambodia (NBC), there is only one empirical study that investigates governance practices in the banking sector (Cheaseth, Samreth, & Sethyraon, 2010). Therefore, more studies are needed to investigate the current governance practices in the banking sector and assess how the practices affect banks' performance. Additionally, comparing the level of corporate governance practice in Cambodia to other ASEAN countries, there is still a need for improvement in terms of corporate transparency, accountability, shareholder protection mechanisms, and improve risk management in Cambodia (Sokhorng, 2016). Without transparency and accountability that ensures good governance, many corporations might go through considerable failures that will surely undermine the general economic development of a country (Jensen, 2001).

The objectives of this study are to investigate the impact of corporate governance instruments on firm performance by using an appropriate proxy of return on asset (ROA) for an emerging economy. The current study makes several contributions to the literature. It provides evidence of how corporate governance affects bank performance by using an appropriate performance proxy. Furthermore, it makes a practical contribution to the management of these banks and the policymakers at large. Therefore, the study will provide new empirical evidence on the influence of corporate governance on bank performance.

## Theoretical and empirical background

Managers have both the ability to commit the organization to any form of contracts and transactions they deem appropriate as they act on behalf of the shareholders. As such there is a need for good corporate governance mechanisms to ensure that the managers are responsible and accountable to shareholders in protecting their interest, hence reducing conflict of interest. A sound and effective governance system in an organization will have an impact on the long-term sustainability of the business and generate greater wealth for the shareholders. Managers should be good stewards whose behaviors are aligned with the objectives of their principals (Davis, Schoorman & Donaldson, 1997; Jensen & Meckling, 1976).

Extensive studies have investigated the relevance of good corporate governance mechanism, such as board tasks, duality, executive compensation, board size and board independence, board committee, and firm value in developed countries for instance, (Coles and Hesterly, 2000; Daily & Dalton, 1994; Elsayed, 2007; Jensen, 1993; Yermack, 1996). However, in frontier markets, there is scant literature to investigate the impact of good corporate governance instruments on firm value, such as the study by Arora and Sharma (2016). To achieve the objectives of this study, further discussions related to the literature and hypothesis development process were discussed in the following section.

Board size is the number of directors on the board. Finding the right board size that affects its capacity to function efficiently and effectively has been a matter of continuing debate (Dalton, Daily, Johnson & Ellstrand, 1999; Hermalin & Weisbach, 2003; Yermack, 1996). The number of directors on a company's board is proved to be a significant indicator of firms' performance. A larger board can increase firms' performance (Anderson & Reeb, 2003; Coles et al., 2008; Klein, 1998). Large board size is associated with having quality advice and counsel to the CEO, thus better performance (Chaganti et al. 1985; Dalton et al. 1999). Moreover, a company with a large board would have access to diverse skills, expertise, and experience from different members to help counsel the CEO effectively on investment opportunities and business improvement (Eisenberg, Sundgren, & Wells, 1998). Having a large board size also enable companies to have access to more resources and information that would assist the management in formulating strategies (Lehn, Sukesh, & Zhao, 2004).

However, on the contrary, some literature finds that board size smaller boards have a stronger relationship between firm performance (Guest, 2009; Jensen, 1993; Wu, 2004; Yermack, 1996). A large number of directors on board is difficult to coordinate. Some directors may not contribute and may tag along as free-riders which reduces the efficiency of the board. A large board could also result in less meaningful discussion, since expressing opinions within a large group is generally time-consuming and difficult (Dalton et al., 1999; Lipton & Lorch, 1992). Instead, Jensen (1993) recommended a small board because of efficiency in decision making due to greater coordination and lesser communication problems. A smaller board of directors is more effective in monitoring and controlling activities as strategic decisions could be made faster (Certo, Richards, & Dalton, 2006).

*H1: There is a relationship between board size and firms' performance.*

Studies have shown that the presence of independent non-executive directors (NEDs) on companies' boards increases overall performance (Dowell et al., 2011; Elloumi & Gueyie, 2001; Guillet et al., 2013; Krause & Semadeni, 2013; Ong & Wan, 2001). This is because NEDs act as business advisers to the board of companies and as well as acting as watchdogs to ensure that the executive directors (EDs) live to their primary responsibilities of maximizing shareholder's wealth. According to Nowak and McCabe (2008), the presence of NEDs on the board would provide a safeguard for a balance of power or management relationship and will provide a variety of independent thinking, and a majority of them could reduce the dangers of 'group think.' NEDs can potentially assist the company during a crisis because the company can have access to useful resources and information and can improve relationships with the external environment facilitate by outside directors (Dowell et al., 2011; Pfeffer & Salancik, 1978). The presence of NEDs would benefit the company to have better access to external resources and management competencies as in some cases the independent directors can replace the managers when necessary (Hillman & Dalziel, 2003; Weisbach, 1988).

However, Kakabadse, Yang, and Sanders (2010) narrated the effectiveness of NEDs in China is determined by their formal independence, information accessibility, incentives provided, and competency. However, they found out that the NEDs system in China was weak because there was too much intervention of controlling shareholders and there was a lack of understanding of the functions of NEDs. Similarly, Wooi and Ming (2009) indicated that the NEDs have failed in their internal monitoring role in Malaysian Government Linked Companies (GLCs).

*H2: There is a relationship between independent non-executive directors and firms' performance.*

According to Fama and Jensen (1983) boards of directors have the fiduciary responsibility of acting on behalf of the shareholders. To effectively monitor executive management and to perform their fiduciary role, the board delegates most of the responsibilities to committees (Adams, 2003; Guo & Masulis, 2015). Some of these committees are formed ad-hoc for a specific task, while some are standing committees delegated with specific and narrowly defined functions. The committees are composed of expertise board members who technically deal with specialized issues that the board as a whole will waste much time handling. Studies have shown that the establishment of a board committee facilitates effective governance (Adams, 2003; Klein, 1998). The number and functions of these committees vary across firms, and roles are sometimes combined. For instance, all firms in the S&P 500 sample have at least one standing committee, with the average firm having three committees. The most common among these committees are the audit committee, the nomination committee, and the compensation committee.

Empirical evidence suggests many board important decisions are made at the board committees and then the recommendations of these committees are placed before the full board for deliberation (Klein, 1998). The establishment of board committees is expected to have a positive effect on corporate performance, but relatively little empirical research has been conducted in this area (McMullen, 1996). There is some empirical evidence on the positive relationship between the independent audit committee and reliable financial reporting (McMullen, 1996). Nevertheless, Klein (1998) could not detect any relationship between the presence of oversight board committees, except finance and investment committees, with the firm performance of the US companies. Similar to their US counterparts, Vafeas and Theodorou (1998) and Dulewicz and Herbert (2004) could not detect any significant relationship with the UK sample.

In Cambodia, commercial banks are required to have only two committees namely, an audit and risk committee by the Prakas on Governance in Bank and Financial Institution of National Bank of Cambodia of 2008. Furthermore, the Prakas also encouraged commercial banks to have a remuneration or a nomination committee (which lies at the bank's discretion). For the sample banks selected, almost all of the firms are having the required audit and risk committee, but not many of them have a remuneration committee or a nomination committee.

*H3: There is a positive relationship between board committees and firms' performance.*

Board diversity suggests that boards should reflect the structure of the society and appropriately represent the gender, ethnicity, and professional backgrounds and experiences that would allow the work of the board to be undertaken most efficiently. Boards are concerned with having the right composition to provide diverse perspectives (Milliken & Martins, 1996; Biggins, 1999). Setting strategic directions, making strategic choices, and supervising management decisions are among the key responsibilities of the board of directors. Doing so requires each board member to be fully equipped with management knowledge such as finance, accounting, marketing, information systems, legal issues, and other related areas to the decision-making process. This requirement implies that the quality of each board member will contribute significantly and positively to management decisions which are then translated into the firm's performance (Nicholson & Kiel, 2004; Fairchild & Li, 2005; Adams & Ferreira, 2007).

Moreover, it is argued that board members with older age will have much more experience compared to a younger age director. They can be valuable resources to firms given their wealth of business experience and professional connections accumulated throughout their long careers. Moreover, since they are most likely to have retired from their full-time jobs, they should have more time available to devote to their board responsibilities (Masulis, Wang,

Xie & Zhang, 2018). Thus, this experience is expected to positively contribute to the better performance of a firm. However, older-age board member appears to be more aggressive and dictatorial with decisions. These characteristics of board members may result in risky decision-making, which may undermine a firm's performance (Carlson & Karlsson, 1970). Older-age directors can face declining energy, physical strength, and mental acumen, which can undermine their monitoring and advisory functions. They can also have less incentive to build and maintain their reputation in the director labor market, given their dwindling future directorship opportunities and shorter expected board tenure as they approach normal retirement age (Masulis et al., 2018). The preceding discussion leads us to formulate the following hypotheses:

*H4: There is a positive relationship between the board's educational level and firms' performance.*

*H5: There is a positive relationship between the board's level of experience and firms' performance.*

## Methodology

### Data

To carry out the present study, the selected horizon period for the study is from 2014 to 2018. Since the study focuses on investigating the relevance of good corporate governance practices to firm value by comparing foreign and domestic owned commercial banks in Cambodia, the study initially includes all the 42 commercial banks operational during the mentioned period under the supervision of the National Bank of Cambodia (NBC). Subsequently, information on these banks was obtained from the following databases:

- From the NBC database, corporate information such as banks' profile information, the balance sheets, and income statements among other records of all commercial banks in Cambodia was obtained.
- From the annual financial statements reports that corporate governances report issued by the different banks. Information such as the number of total directors, the number of independent directors, and the number of female directors was obtained. With all this information in hand, the study approximates the size of the board by the number of directors that it contains; estimate the independence through the relative importance of the number of independent non-executive directors relative to the total number of directors on the board.

To form part of the sample, the bank's data must be available during the period of study. Banks with unavailable financial performance data or governance data were excluded. After vetting through the availability of data, the number of commercial banks that make up the final sample consists of a balanced panel data of 35 firms with 491 observations.

### Model

The model used in this study is adopted from the previous studies of Bhat, Chen, Jebran, and Bhutto (2018) and Rashid and Islam (2013). The data set in this study contains pooled observations on cross-section and time-series data. To estimate such a pooled data model, we use the panel data techniques which may be written as:

$$Y_{it} = \alpha + X_{it}\beta + \delta_i + \lambda_t + \mu_{it}; i = 1, 2, \dots, N; \text{ and } t = 1, 2, \dots, T \quad (1)$$

where;

$Y_{it}$  is the dependent variable;

$\alpha$  represent the overall constant in the model;

$X_{it}$  is a k-vector of regressors;

$\delta_i$  represent cross-section specific effects;

$\lambda_t$  represent period-specific effects;

$\mu_{it}$  is the error terms;

$i$  is the number of cross-section units (firm); and

$t$  is the number of periods.

A panel regression models have been formulated to examine the relationship of corporate governance mechanism and firm value. Thus equation (1) can be rewritten as follows:

$$Y_{it}^j = \beta_0 + \beta_1 BDS_{it} + \beta_2 NED_{it} + \beta_3 BCM_{it} + \beta_4 BED_{it} + \beta_5 BEP_{it} + \beta_6 LTA_{it} + \beta_7 EFF_{it} + \alpha_i + \lambda_t + \mu_{it} \quad (2)$$

where;

$Y$  denotes firm performance;

$j$  ROA; and

$i$  2014, 2015, 2016, 2017 and 2018.

### Description of Variables

In the multiple regression models, the firm performance is measure as return on asset (ROA) is the dependent variable, board size, non-executive director, board committees and board member experience are explanatory variables, and firm size as control variables. Board size (BSZ) is the number of executives and non-executive directors on the board, non-executive director (NED) is the proportion of non-executive directors on the board at the year-end, board committee (BCM) is a dummy variable that equals 1 if the bank is having more board committees more than the required two board committees by NBC, otherwise zero, board experience (BEP) is the average age of all directors on the board and board education level (BED) is the number of directors with postgraduate degrees. Firm-specific characteristics which are considered to affect firm performance such as firm size (LTA) and firm efficiency (EFF) have also been incorporated into the model. The definition of variables in the panel regression models is given in table 1.

Table 1: Variables measurement

Variables	Definition	Measurement
<b>Dependent variables</b>		
ROA	Return on asset	Net profit for the year to total assets.
<b>Explanatory variables</b>		
BSIZE	Board size	Many executive and non-executive directors on the board.
NEDs	Non-executive director	The proportion of Non-executive directors on the board at the year-end.
BEXP	Board member's working experience	The average age of all directors on the board.
BEDU	Board member's educational level	Several directors with postgraduate degrees or professional qualifications.
BCMT	Board committees	Dummy variables that equal 1 if the bank is having more board committees more than the required two board committees by NBC, otherwise zero.
<b>Control variables</b>		
EFFC	Bank's efficiency	The ratio of interest income plus non-interest income to the total asset.
LTA	Bank size	Natural logarithm of the book value of total assets.

Board size (BSIZE), Non-executive directors (NEDs), Board committees (BCMT), Board member education (BEDU), Board member experience (BEXP), Natural logarithm of the total asset (LTA), Bank's efficiency (EFFC).

### Statistical Analysis

A descriptive analysis was carried out to understand the mean differences of the variables used in the samples. Then, diagnostic tests were carried out, such as the Pearson correlation test is conducted among the explanatory variables to check for multicollinearity (Bhat et al., 2018; Rashid & Islam, 2013). Panel ordinary least square with random-effects and fixed-effects is applied on two data sets to investigate the relationship between dependent and

independent variables. Suitable panel regression for both data sets is determined based on the Hausman test (Hausman, 1978) and Breusch–Pagan test (Breusch & Pagan, 1979). The Hausman test can help you to choose between a fixed-effects model or a random-effects model. The null hypothesis is that the preferred model is random effects; The alternate hypothesis is that the model has fixed effects. The Hausman test also generates a chi-squared probability and if that value is greater than the significant value (5%) then the null hypothesis is accepted (Chmelarova, 2007). This is important when analyzing panel data to achieve robust results for variables that have been omitted or not considered. The econometric model used in this study has been used in many previous studies such as by Arora and Sharma (2016) and Bhat et al. (2018).

## Results and Discussions

### *Descriptive Analysis*

Table 1 present the descriptive statistics for the variables used, grouped by the characteristics of the board analyzed, the performance of the firm, and other variables of interest that will be used as control variables. The statistics for the sample firms, including mean, standard deviation, and standard error of the mean for all banks in the sample. The mean value of ROA is 0.014, on average, the sample banks have a board size of 7.68 of which around 52.33 percent of the directors are non-executive directors. It can therefore be established that banks in Cambodia also have a substantially higher percentage of NEDs on their board, which supports the idea of agency theory by reducing the conflict of interest that insider directors may have. Based on the mean value, it is likely that Cambodian banks will establish more board committees high than the required two committees namely audit and risk committee as per the Prakas on governance for commercial banks. Consequently, a conclusion can be made that there is a high implementation of governance procedures of this mechanism. Furthermore, on average, 2.57 of the board members are having a postgraduate degree and the average experience of the board members is around 42.24 years. The mean value of the ratio of non-performing loans to total loans is 34.97 percent while the mean value of the bank size is 14.33.

Table 2: Summary of the descriptive statistics.

Variables	Mean	Std. Dev.	Std. Error Mean	Prob.	Collinearity Statistics	
					Tolerance	VIF
ROA	0.0143	0.014	0.001	0.002***	-	-
BSIZE	7.6827	3.097	0.257	0.5084	0.847	1.180
NEDs	0.5233	0.233	0.019	0.038**	0.834	1.200
BCMT	0.5893	0.495	0.041	0.0813*	0.941	1.062
BEDU	2.5724	0.963	0.080	0.1580	0.850	1.177
BEXP	42.241	10.01	0.832	1.6435	0.902	1.108
LTA	14.333	1.622	0.135	0.2611	0.835	1.198
EFFC	0.3497	0.952	0.079	0.016***	0.928	1.078

\*, \*\*, \*\*\* significant at 10 percent, 5 percent, and 1 percent levels respectively. Board size (BSIZE), Non-executive directors (NEDs), Board committees (BCMT), Board member education (BEDU), Board member experience (BEXP), Natural logarithm of a total asset (LTA), Bank's efficiency (EFFC). The number of observations is 145.

Moreover, a Pearson correlation test was employed to investigate the relationship between the independent variables, and the results are summarized in Table 3. The findings show that the correlations among the variables are relatively low ranging from -0.007 to 0.162. To further verify that multicollinearity is not a problem in this study, a variance inflation factor (VIF) was reported in Table 2. If the variables have VIF values greater than 10, or tolerance values lower than 0.10, then they were considered to have multicollinearity problems (Gujarati, 2003). Since all the variables had VIF values ranging from 1.062 to 1.200 shown in table 2, hence, the results suggest that there was no multicollinearity problem in the study. Therefore, all the independent variables can be used within the regression model (Gujarati & Porter, 2009).



Table 3: Pearson correlation analysis

	BSIZE	NEDs	BCMT	BEDU	BEXP	LTA	EFFC
BSIZE	1						
NEDs	-0.288**	1					
BCMT	-0.083	-0.102	1				
BEDU	0.138	-0.122	-0.074	1			
BEXP	-0.043	0.162	-0.180*	-0.081	1		
LTA	0.089	0.164*	-0.036	-0.324**	0.160	1	
EFFC	0.120	0.088	-0.007	0.125	-0.153	-0.019	1

\*, \*\*, \*\*\* significant at 10 percent, 5 percent, and 1 percent levels respectively. Board size (BSIZE), Non-executive directors (NEDs), Board committees (BCMT), Board member education (BEDU), Board member experience (BEXP), Natural logarithm of the total asset (LTA), Bank's efficiency (EFFC).

Furthermore, to examine which model is appropriate, the study conducted Hausman and Breusch–Pagan test on the data set. The results from the Hausman test emphasized the use of the random-effects model since the  $\chi^2$  (7) is 12.88 with a  $\text{prob} > \chi^2 = 0.075$  is greater than 0.05, as such the null hypothesis confirms that the preferred model is the random-effects model. Similarly, the result of the Breusch–Pagan test shows a  $\text{chibar}^2$  (01) of 21.26 with a  $\text{prob} > \text{chibar}^2$  of 0.000, thus supporting the use of a random-effect model. Therefore, this study will run the random-effects model using generalized least square (GLS) regression to examine the relevance of good corporate governance practices on bank performance. The random-effects model refers to a model with non-different (constant) slope but with varying or different intercepts based on cross-section (in this case is the banks) randomly instead of in a fixed manner (Gujarati, 2004).

The results of the GLS regression are shown in table 4. The result shows that there is enough evidence at a statistical significance level of 5 percent for BEDU to have a positive impact on a bank's performance. This means that an increase of one board member with a postgraduate degree or professional qualification is expected to increase the performance of the banks on average by 0.216. The finding supports hypothesis 4 and consistent with previous studies (Adams & Ferreira, 2007; Berger, Kick & Schaeck, 2014; Fairchild & Li, 2005; Nicholson & Kiel, 2004) emphasizing that a higher level of board member's qualification will enable them to steer the company in the right direction by making better corporate decisions. Setting strategic directions, making strategic choices, and supervising management decisions are among the key responsibilities of the board of directors. Therefore, a board member should be fully equipped with business management knowledge such as finance, accounting, marketing, information systems, legal issues, and other related areas relevant to the decision-making process (Berger et al., 2014; Khanchel, 2007; Nicholson & Kiel, 2004). This requirement implies that the quality of each board member will contribute immensely to the management decisions which if successful will then translated into the firm's performance.

Table 4: Results of Random-effect GLS Regression Model

Variables	Coefficient	Std. Error	t-statistics	Prob.
<i>Constant</i>	-0.030	0.01464	-2.268	0.025**
BSIZE	-0.033	0.00058	-0.371	0.071*
NEDs	0.066	0.00783	0.739	0.461
BEXP	0.085	0.00174	1.020	0.309
BEDU	0.216	0.01188	2.446	0.016***
BCMT	0.085	0.00217	0.994	0.032**
EFFC	0.225	0.01153	2.532	0.012***
LTA	0.096	0.00077	1.136	0.258
<b>Model Test Results</b>				
R <sup>2</sup>	0.3561			
Adjusted R <sup>2</sup>	0.2156			
Wald Chi <sup>2</sup>	7.79*			
sigma_u	0.0245			
sigma_e	0.0116			
rho	0.8150 (fraction of variance due to u_i)			

\*, \*\*, \*\*\* significant at 10 percent, 5 percent, and 1 percent levels respectively. Board size (BSIZE), Non-executive directors (NEDs), Board committees (BCMT), Board member education (BEDU), Board member experience (BEXP), Natural logarithm of the total asset (LTA), Bank's efficiency (EFFC).

Furthermore, the findings show that BCMT has a positive impact on bank performance and is statistically significant at a 5 percent level. The result indicates an increase in board committees will result in a higher bank performance on average by 0.085. The result supports hypothesis 3 and is in line with previous studies (Lam & Lee, 2012; McMullen, 1996; Sanchez, Odriozola & Luna, 2020) where empirical findings reveal that board committee (especially nomination committee) is positively related to firm performance. Having several board committees significantly improving banks' accountability and transparency by reducing individual free-riding and enabling outside directors to perform their monitoring duties more effectively through greater separation from management (Chen & Wu, 2016). It will also reduce the CEO's bargaining power as the committee members especially outsider directors be insulated from the CEO's influence. Moreover, having some committees through the process of decentralization will allow for knowledge specialization (De Kluyver, 2009) thereby benefiting firms because the monitoring and advising tasks of boards are complex and require firm-specific knowledge (Kim et al., 2014). Having many board committees will bring about specialization and allow for a more efficient task allocation to directors, leading to task-division efficiency and consequently improving the firm's performance.

Additionally, BSIZE is statistically significant and negatively correlated with bank performance. The result indicates that a smaller board of directors is associated with higher bank performance. A decrease of one board member could potentially increase bank performance by 0.033. The finding is in line with hypothesis 1 and consistent with previous studies (Bhat et al., 2018; Hermalin & Weisbach, 2003; Khanchel, 2007; Ma'aji, Abdullah & Karen, 2019; Ma'aji, Abdullah & Karen, 2018). Smaller board sizes are better than larger ones that may be the plague with free rider and monitoring problem and therefore are expected to experience fewer communication and coordination problems, thus improving performance (Hermalin & Weisbach, 2003; Khanchel, 2007; Ma'aji et al., 2019; Ma'aji et al., 2018). From the sampled banks, some of the banks are having board members ranging from 17 to 15 people. This could potentially result in less meaningful discussion, since expressing opinions within a large group is generally time-consuming and difficult (Dalton et al., 1999; Lipton & Lorch, 1992). Therefore, a smaller board would be more effective in monitoring and controlling activities as strategic decisions could be made faster (Certo, Richards, & Dalton, 2006). Ma'aji et al. (2019) also found that smaller board size is associated with reducing the probability of bankruptcy among companies. However, NEDs and BEXP are both having a positive impact on bank performance but not statistically significant.

Moreover, control variables bank efficiency (EFFC) has a positive and statistically significant relationship with a performance at a 5 percent level. This suggests that the higher the efficiency of the banks, the higher the bank performance. Bank size (LTA) as a control variable is having a positive relationship with firm performance but the correlation is not statistically significant. However, through the correlation matrix, various governance factors are having a positive relationship such as BSIZE, NEDs, and BEXP with the size of the bank. For example, it is widely accepted that larger firms are more likely to have larger boards (see, for example, Cicero, Wintoki, & Yang, 2008).

## Conclusion

This section summarized the main findings of the research. The study has conducted empirical research on the relevance of good corporate governance practices to bank's performance. The research contributions are two folds. First, the descriptive analysis of the bank dataset documents several interesting features about the corporate governance practices among banks in Cambodia. Over the study period between 2014 to 2018, banks in Cambodia have seen on average an increase in profitability. Furthermore, banks are having a substantially higher percentage of NEDs on their board, there is a high implementation of governance procedures on board committees were on average banks in Cambodia are having more than the required two board committees (audit and risk committees) as per required by the Prakas on the governance of banks by NBC. The average board size is around eight members of which at least three members are having a postgraduate degree or a professional qualification.

Secondly, GLS regression analysis sheds light on the influence of corporate governance practice on bank performance. The study finds that having a board member with a postgraduate degree or a professional qualification is expected to increase bank performance. Similarly, having some number of board committees will result in a higher bank performance while a smaller board size is associated with higher bank performance. Non-executive directors and the experience of a board member are found to have a positive impact on bank performance but not statistically significant.

### **Recommendations**

Through the cause of this study, we observed that some banks in Cambodia are subsidiaries of a conglomerate and they use the same directors from those businesses that are unrelated to the bank industry. Therefore, the directors lack experience in the new venture and will not contribute to a meaningful board room discussion as it not their area of expertise. For example, some executive board members are medical doctors, engineers by profession and lack any professional qualification that is related to banking which could have helped them to contribute more to board deliberations. Policymakers will have to improve on their supervisory function and role as the majority of the domestic and some foreign banks are not disclosing their annual reports on their respective company website as required by the Prakas on CG of Banks. This will not enable shareholders, investors, and the bank's creditor to make timely and inform investment decisions. More amendments should be made to the current CG Code on financial institutions as the guidelines provided are too general and lack explanatory notes that would interpret and guide banks towards successful compliance and therefore open to individual interpretations and encourage subjective interpretation of the Code. Lawton and Nestor (2010) argued that very few jurisdictions had devised extensive bank-specific governance requirements.

Furthermore, there is also a need for the foreign banks to also implement the local CG requirements to improve consistency and uniformity among the banks in Cambodia. Policymakers should develop a policy that will require foreign banks in Cambodia to follow the strictest rules of governance between Cambodia or the home country of the parent company (and they should disclose information on the CG of their country on their website). Currently, the Prakas did not recommend best practices of hiring executives and NEDs to the board. Therefore, there should be recommendations of best practices for the directors' education qualifications and relevant experiences.

This paper opens many potential future avenues for research. In particular, more empirical and theoretical work is needed to understand information sharing in the context of the board of directors. Besides, it would be desirable to understand why specific committees, such as the strategy and technology committee, are rarely used and how they may impact performance. Moreover, it would be interesting to further examine how the use of board committees can lead to independent decision-making, lowering agency costs among others.

### **Acknowledgment**

This research is fully supported by CamEd Business School, Phnom Pehn Cambodia, therefore the authors wish to express their gratitude to CamEd Business School for the financial support.

### **References**

- Adams, R. (2003). What do boards do? Evidence from board committee and director compensation data. Unpublished working paper. Federal Reserve Bank of New York, New York, NY.
- Albrecht, W. (2016). Why good corporate governance is so important. BYU Wheatley Institution, Working Paper, [https://wheatley.byu.edu/why-good-corporate-governance-is-so-importan t/](https://wheatley.byu.edu/why-good-corporate-governance-is-so-importan-t/)
- Andrianova, S., Demetriades, P., & Shortland, A. (2008). Government ownership of banks, institutions, and financial development. *Journal of development economics*, 85(1-2), 218-252.
- Arora, A., & Sharma, C. (2016). Corporate governance and firm performance in developing countries: evidence from India. *Corporate governance*.
- BCBS (2006) Enhancing Corporate Governance for Banking Organisations. Basel: Bank for International Settlements.

- Berger, A.N., Kick, T., Schaeck, K. (2014). Executive board composition and bank risk-taking. *Journal of Corporate Finance*, 28, 48-65.
- Berger, A. N., Klapper, L. F., Peria, M. S. M., & Zaidi, R. (2008). Bank ownership type and banking relationships. *Journal of Financial Intermediation*, 17(1), 37-62.
- Bhat, K., Chen, Y., Jebran, K., & Bhutto, N. (2018). Corporate governance and firm value: a comparative analysis of state and non-state-owned companies in the context of Pakistan. *Corporate Governance: The International Journal of Business in Society*
- Burlaka, M. V. (2006) 'Bank Corporate Governance: The Emerging Ukrainian Market Compared to International Best Practices,' *Fordham Journal of Corporate & Financial Law*, 11(4), 851–891.
- Breusch, T. S., & Pagan, A. R. (1979). A simple test for heteroscedasticity and random coefficient variation. *Econometrica: Journal of the Econometric Society*, 1287-1294.
- Cheaseth, S., Samreth, S., & Sethyraon, I. (2010). Board governance regulation, practices and their relationships with financial performance: Cambodian bank and microfinance institution context. *The First Annual Online International Conference on Corporate Governance & Regulation in Banks*, Sumy, Ukraine, May 27 – June 2, 2010.
- Cheng, X., & Degryse, H. (2010). The impact of bank and non-bank financial institutions on local economic growth in China. *Journal of Financial Services Research*, 37(2-3), 179-199.
- Chen, D., & Wu, A. (2016). The structure of board committees. Working Paper 17-032, available at [https://www.hbs.edu/faculty/Publication%20Files/17-032\\_22ea9e7a-4f26-4645-af3d-042f2b4e058c.pdf](https://www.hbs.edu/faculty/Publication%20Files/17-032_22ea9e7a-4f26-4645-af3d-042f2b4e058c.pdf)
- Chmelarova, V. (2007). The Hausman test, and Some Alternatives, with Heteroskedastic Data. Louisiana State University and Agricultural & Mechanical College, 2007. Retrieved 1/6/2007 from here ([http://etd.lsu.edu/docs/available/etd-01242007-165928/unrestricted/Chmelarova\\_dis.pdf](http://etd.lsu.edu/docs/available/etd-01242007-165928/unrestricted/Chmelarova_dis.pdf)).
- Cicero, D., Wintoki, M. B., & Yang, T. (2008). Do firms adjust to a target board structure? Unpublished working paper, University of Georgia.
- Coles, J. W., & Hesterly, W. S. (2000). Independence of the chairman and board composition: Firm choices and shareholder value. *Journal of Management*, 26(2), 195-214.
- Cornett, M.M., Marcus, A.J. & Tehranian, H. (2008). Corporate governance and pay-for-performance: The impact of earnings management, *Journal of Financial Economics*, 87, (2): 357-373.
- Daily, C.M. & Dalton, D.R. (1994). Bankruptcy and corporate governance: The impact of board composition and structure, *Academy of Management Journal*, 37: 1603-1617.
- Davis, J. H., Schoorman, F. D., & Donaldson, L. (1997). Toward a stewardship theory of management. *Academy of Management Review*, 22(1), 20-47.
- Demitriades PO, Du J, Girma S, Xu S (2008) Does the Chinese Banking System Promote the Growth of Firms? University of Leicester Discussion Paper 08/6.
- Dulewicz, V. and Herbert, P. (2004). Does the composition and practice of boards of directors bear any relationship to the performance of their companies? *Corporate Governance: An International Review*, 12(3), 263-80.
- Elsayed, K. (2007). Does CEO duality affect corporate performance? *Corporate Governance: An international review*, 15(6), 1203-1214.
- Fama, E., & Jensen, M. (1983). Separation of ownership and control. *Journal of Law and Economics*, 26, 301-325.
- Gebba, T. R. (2015) 'Corporate Governance Mechanisms Adopted by UAE National Commercial Banks', *Journal of Applied Finance & Banking*, 5(5), 23–61.
- Guest, M. (2009): The impact of board size on firm performance: evidence from the UK, *The European Journal of Finance*, 15:4, 385-404.
- Guillet, B.D., Seo, K., Kucukusta, D. & Lee, S. (2013). CEO duality and firm performance in the US restaurant industry: Moderating role of restaurant type, *International Journal of Hospitality Management*, 33: 339-346.
- Gujarati, D. (2004). *Basic Econometric* (Trans. S. Zain). Jakarta: Erlangga Publishers.
- Guo, L., & Masulis, R.W. (2015). Board Structure and Monitoring: New evidence from CEO turnovers. *Review of Financial Studies*, 28(10), 2770-2811.
- Hausman, J. A. 1978. Specification tests in econometrics. *Econometrica* 46: 1251–1271.
- Jensen, M. (2001). Value maximization, stakeholder theory, and the corporate objective function. *Journal of applied corporate finance*, 14(3), 8-21.
- Jensen, M., & Meckling, W. (1976). Theory of the firm: Management behavior, agency costs, and capital structure. *Journal of financial economics*, 3(4), 305-60.
- Kakabadse, N. K, Yang, H. & Sanders, R. (2010). The effectiveness of non-executive directors in Chinese state-owned enterprises. *Management Decision*, 48(7), 1063-1079
- Kirkpatrick, G. (2009) 'The Corporate Governance Lessons from the Financial Crisis, *Financial Market Trends*, 2009 (1), 61–87.
- Klein, A. (1998). Firm performance and board committee structure. *Journal of Law and Economics*, 41(1), 275-303.

- Krause, R. & Semadeni, M. (2013). Apprentice, departure, and demotion: An examination of the three types of CEO–board chair separation, *Academy of Management Journal*, 56(3), 805-826.
- Laeven, L. (2013) ‘Corporate governance: What’s special about banks?’, *Annual Review of Financial Economics*, 5(1), 63–92.
- Macey, J. R., & O'hara, M. (2003). The corporate governance of banks. *Economic policy review*, 9(1).
- Ma'aji, M., Abdullah, N., & Khaw, K. (2018). Predicting Financial Distress among SMEs in Malaysia. *European Scientific Journal*, 14, 91.
- Ma'aji, M., Abdullah, N., & Khaw, K. (2019). Financial distress among SMEs in Malaysia: An early warning signal. *International Journal of Business & Society*, 20(2), 775-792.
- Marcinkowska, M. (2012) ‘Corporate Governance in Banks: Problems and Remedies’, *Financial Assets and Investing*, 2 (2), 47–67.
- Masulis, R. W., Wang, C., Xie, F., & Zhang, S. (2018). Directors: Older and Wiser, or Too Old to Govern? *European Corporate Governance Institute (ECGI)-Finance Working Paper*, (584).
- Maxfield, S., Wang, L. and Magaldi de Sousa, M. (2018) ‘The Effectiveness of Bank Governance Reforms in the Wake of the Financial Crisis: A Stakeholder Approach’, *Journal of Business Ethics*, 150(2), 485–503.
- McMullen, D.A. (1996). Audit committee performance: an investigation of consequences associated with audit committees. *Auditing: A Journal of Practice and Theory*, 15(1), 87-103.
- Nowak, M. & McCabe, M. (2008). The independent director on the board of company directors. *Managerial Auditing Journal*, 23(6), 545-566
- OECD (2015). G20/OECD principles of corporate governance. OECD Publishing, Paris.  
<http://dx.doi.org/10.1787/9789264236882-en>
- Ong, C., Wan, D. Board Structure, Board Process, and Board Performance: A Review & Research Agenda. *Journal of Comparative International Management*, 4(1), 3-24.
- Pagano, M., & Volpin, P. F. (2005). The political economy of corporate governance. *American economic review*, 95(4), 1005-1030.
- Rashid, K. & Islam, S. (2013). Corporate governance, complementarities and the value of a firm in an emerging market: the effect of market imperfections. *Corporate Governance: The International Journal of Business in Society*, 13(1), 70-87.
- Sanchez, L., Odriozola D., & Luna, M. (2020). How corporate governance mechanisms of banks have changed after the 2007–08 financial crisis. *Global Policy*, 11(1), 52 – 61.
- Shleifer, A., & Vishny, R. W. (1997). A survey of corporate governance. *The journal of finance*, 52(2), 737-783.
- Sokhorn, C. (2016). Firms flimsy on corporate governance. *Phnom Penh Post News* <https://www.phnompenhpost.com/business/firms-flimsy-corporate-governance>
- Stein, E., & Daude, C. (2001). Institutions, integration, and the location of foreign direct investment. *New horizons for foreign direct investment*, 101.
- Talamo, G. M. C. (2009). 2. FDI, mode of entry and corporate governance. *Geography, Structural Change, and Economic Development: Theory and Empirics*, 29.
- Talamo, G. (2011). Corporate governance and capital flows. *Corporate Governance: International Journal of Business in Society*, 11(3), 228-243.
- Vafeas, N. & Theodorou, E. (1998). The relationship between board structure and firm performance in the UK. *British Accounting Journal*, 30, 383-407.
- Wooi, H. C & Ming, T. C (2009). Directors’ Pay-Performance: A Study on Malaysian Government Linked Companies. *CenPRIS Working Paper No. 110/09*, Universiti Sains Malaysia
- Wu, Y. (2004). The impact of public opinion on board structure changes, director career progression, and CEO turnover: Evidence from CalPERS’ corporate governance program. *Journal of Corporate Finance*, 10, 199–227.
- Yermack, D. 1996. Higher market valuation of companies with a small board of directors. *Journal of Financial Economics* 40: 185–221.
- Zakaria, Z., Purhanudin, N. and Wahidudin, A. N. (2018) ‘The Role of Board Governance on Bank Performance,’ *Journal of Finance & Banking Studies*, 7(4), 38–50.