BOARD CHARACTERISTICS AND FIRM PERFORMANCE OF PUBLIC LISTED COMPANIES IN MALAYSIA

FAISAL ABUKAR H-SUFI

UNIVERSITI UTARA MALAYSIA

2012

BOARD CHARACTERISTICS AND FIRM PERFORMANCE OF PUBLIC LISTED COMPANIES IN MALAYSIA

A thesis submitted to College of Business in partial fulfillment of the requirement

for postgraduate Master of Science of International Accounting

Universiti Utara Malaysia

By

Faisal Abukar H-Sufi (808827)

UNIVERSITI UTARA MALAYSIA

2012

DECLARATION

I hereby certify that the substance of this thesis has not been already submitted to any degree and is not currently being submitted for any other qualification.

I certify that any assistance received in preparing this thesis and all sources used have been acknowledged and referenced in this thesis.

Faisal Abukar H-Sufi

808827

College of Business

University Utara Malaysia

06010 Sintok

Kedah

PERMISSION TO USE

In preparing this thesis in partial fulfilment of the requirements for a postgraduate degree from Universiti Utara Malaysia (UUM), I agree that Universti library may make it unreservedly available for inspection. I further agree that permission for copy of this thesis in any manner, in whole or in part, for scholarly purposes may be granted by my supervisor Dr. Hasnah Kamardin or, in her absence by the college of Business Dean. It is understood that any copying or publishing or using of this thesis or parts thereof for financial gain shall not be allowed without any written permission. It is also understood that due recognition shall be given to me and to Universiti Utara Malaysia for any scholarly use which may be made of any material from this thesis.

Request for permission to copy or to make other use of material in this thesis, in whole or in part, should be addressed to:

Dean

College of Business

Universiti Utara Malaysia

06010 Sintok

Kedah Darul Aman

ABSTRACT

The study aims to investigate the influence of board characteristics on firm performance before and after the revised of Malaysian Code of Corporate Governance 2007. The data for study gathered from two years, 2006 and 2010, that represent before and after the revised version of Malaysian Code of Corporate Governance. Regression analysis was performed to examine factors influencing firm performance such as board size, outside directors, family members on the board, audit committee size, audit committee independent, control variables such as firm size, leverage, and firm performance. In addition, firm performance was measured by return on asset (ROA). Using a sample of 80 companies for both years, the result showed that none of the board characteristics, board size, independent directors, family members on the board, audit committee size, audit committee independent, have significant relationship with firm performance. However, the control variables, firm size and leverage, have significantly positive and negative correlation with firm performance in both years.

AKNOWLEDGMENTS

In the name of Allah the Most gracious and Most Merciful. Praise all is to Allah, the creator of this Universal and His Messenger, Muhammad, peace and blessings of Allah are upon him. I am very grateful and feel thankful to Allah for the blessings, guidance, strength and health that he has given me during my study period that without his Mercy, it would have been impossible for me to complete my thesis as required.

Firstly, I wish to express my sincere gratitude to my supervisor, Dr. Hasnah Kamadin for her support, guidance, time, and spirit. Actually I obtained valuable experience, knowledge, hardworking with her and I feel honoured and grateful to work under her supervision. I am also gratitude to everyone who involved and contributed during my preparation and completion of my thesis. I also feel gratitude to Simad University for giving me the opportunity and scholarship to pursue my graduate study.

Secondly, I would like to express my sincere recognition and gratitude to all my dear friends who have contributed and supported me during the period of my thesis work. Special credit goes to Abdifatah Ahmed Haji, Mohamed Omar Abdulahi and Mohamed Bashir Mohamed

Finally, I would like to say gratitude to my beloved family. To my parents – Abukar Haji Sufi, Habibo Eli Awale peace and blessing of Allah be up them; my uncle - Awil Elmi Awale and my aunt - Khadijo Abdulle Khawane; my brothers - Abas Abukar Haji, and Abdulkadir Abukar Haji; my sisters -Muno Awil Elmi, Idil Awil Elmi, Bibi Abukar Haji, Warsan Abukar Haji, Istar Abukar Haji, Sucdi Abukar Haji, Hamdi Abukar Haji, Fartun Abukar Haji, and my nephews - Hasan Abdurrahman Hassan and Awil Abdurrahman Hassan.

TABLE OF CONTENTS

CHAPTER THREE: THEOROTICAL FRAMEWORK AND METHODOLOGY

LIST OF TABLES

LIST OF FIGURES

LIST OF ABBREVIATIONS

MCCG	Malaysian code of corporate governance
FP	Firm Performance
BSIZE	Board size
INDS	Independent directors
FMB	Family members on the board
AUCSIZE	Audit committee size
AUTCID	Audit committee independent
FSIZE	Firm size
LRAGE	Leverage

CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

With increasing trends towards globalization and quick growth of companies, the need of corporate governance structure, spread throughout the world in order to enhance firm performance. These changes attracted the attention of potential investors, who had already lost market confidence, to make wisely investment decision. If the company's corporate governance strategy towards its performance is very poor, it will lose large market shares of the business and it will also miss the game. Recent financial crisis have renewed attention to corporate governance and it is recognized that firms having better corporate governance structures signals better performance (Chiang, 2005).

In the last two decades the importance of corporate governance increased due to the high-profile collapses of a number of large corporations, most of which involved accounting fraud. In the multinational companies, managers may make decision that conflict with the firm's goal to maximize shareholder wealth, for example a decision to expand a subsidiary may be motivated by a manager's desire to receive more compensation rather than to enhance the value of the firm. These personal conflicts can be reduced if clear and proper corporate governance is set up (Madura, 2010).

In order to understand broadly the issues of corporate governance, it is very important to study the role of corporate governance in this matter. Corporate governance is defined as a "system that enhances the relationship between companies' managers, its board of directors, its potential shareholders, and other stakeholders and it also provides proper allocation of the resources among the competitive uses. In addition to that, it provides structure through which

The contents of the thesis is for internal user only

References

Abbott, J. L., Park, Y., and Parker, S. (2000). The effects of audit committee activity and independence on corporate fraud. *Managerial Finance , 26* (11), 550-68.

Abdullah, S. N. (2004). Board Composition, CEO Duality and Performance among Malaysian Listed Companies. *Corporate Governance , 4* (4), 47-61.

Abidin, Z. Z., and Kamal, N. M. (2009). Board Structure and Corporate Performance in Malaysia. *International Journal of Economics and Finance , 1* (1), 150--164.

Amran, N. A. (2011). Corporate Governance Mechanisms and Company Performance: Evidence from Malaysian Companies. *International Review of Business Research Papers , 7* (6), 101-114.

Baek, J.-S., Kang, J.-K., and Park, K. S. (2004). Corporate governance andfirm value: evidence from the Korean financial crisis. *Journal of Financial Economics , 71*, 265-313.

Bakar, N. B., Rahman, A. R., and Rashid, H. M. (2005). Factors influencing auditor independence: Malaysian loan officers' perceptions. *Managerial Auditing Journal , 20*, 804-822.

Bhimani, A. (2008). Making Corporate Governance Count: The Fusion of Ethics and Economic Rationality. *Journal of Management and Governance , 12* (2), 135-147.

Cadbury, R. (1992). Report of the Committee on Financial Aspects of Corporate Governance. London:. *Gee Publishing* .

Carcello, J. V., and Neal, T. L. (2000). Audit Committee Composition and Auditor Reporting. *The Accounting Review , 75* (4), 453-467.

Chen, Z., Cheung, Y.-L., Stouraitis, A., & Wong, A. W. (2005). Ownership concentration, f irm performance, and dividend policy in Hong Kong. *Pacific-Basin Finance Journal , 13*, 431-449.

Cheng, S. (2008). Board Size and The Variability of Corporate Performance. *Journal of Financial Economics , 87*, 157-176.

Chiang, H. (2005). An Emperical Study of Corporate Governance and Corporate Performance. *Journal of American Academy of Business , 1*, 95-101.

Claessens, S., Djankov, S., and Lang, L. H. (2000). The separation of ownership and control in East Asian Corporations. *Journal of Financial Economics , 58*, 81-112.

Coles, J. L., Daniel, N. D., and Naveen, L. (2008). Boards: Does one size fit all? *Journal of Financial Economics , 87*, 329-356.

Conyon, M. J., and Peck, S. I. (2010). Board size and corporate performance: evidence from European countries. *The European Journal of Finance , 4* (3), 291-304.

Conyon, M. J., and Pecks, S. I. (1998). Boar Size and Corporate Governance: Evidence from European Countries. *The European Journal of Finance , 4,* 291-304.

Corporate, G. B. (2011). *Towards Excellence in Corporate Governance.*

Cotter, J. F., Shivdasani, A., and Zenner, M. (1997). Do Independent directors enhance target shareholders wealth during tender offers. *Journal of Financial Economics , 43,* 195-218.

Dahya, J., Dimitrov, O., and McConnell, J. J. (2008). Dominant shareholders, corporate boards, and corporate value: A cross-country analysis. *Journal of Financial Economics , 87*, 73-100.

Daily, C. M., Dalton, D. R., and Canella, A. A. (2003). Corporate Governance: Decades of Dialogue and Data. *Academy of Management Review, , 28* (3), 371-382.

Dehaen, A., Vuyst, V. D., and Ooghe, H. (2001). Board Structure in Belgian. *LRP journal* (34), 383-398.

Doupnik, T., and Perera, H. (2008). *International Accountin.* McGraw-Hill.

Eisenberg, T., Sundgren, S., and Wellss, M. T. (1998). Larger Boar Size and Decreasing Firm Value in Small Firms. *Journal of Financial Economics , 48,* 35-54.

Eisenhardt, K. M. (1989). Agency theory: an assessment and review. *Academy of Management Review , 14* (1), 57-74.

Fama, E. F., and Jensen, M. C. (1983). Separation ownersip and Control. *Journal of Law and Economics* , 327-349.

Felo, A. J., Krishnamurthy, S., and Solieri, S. A. (2003). Audit Committee Characteristics and the Perceived Quality of Financial Reporting: An Empirical Analysis . *Journal of Accounting and Publick Policy* , 1-37.

Filatotchev, I., Lien, Y.-C., and Piesse, J. (2005). Corporate Governance and Performance in Publicly Listed, Family-Controlled Firms: Evidence from Taiwan. *Asia Pacific Journal of Management , 22*, 257–283.

Ghazali, N. A. (2010). Ownership Structure, Corporare Governance and Corporate Performance. *International Journal Commerce and Management , 20* (2), 109-119.

Goodwin, J., and Yeo, T. Y. (2001). Two Factors Affecting Internal Audit Independence and Objectivity: Evidence from Singapore. *International Journal of Auditing , 5*, 107-125.

Guay, W. R. (1999). The sensitivity of CEO wealth to equity risk: an analysis of the magnitude and determinants. *Journal of Financial Economics , 53*, 43-71.

Gujarati, D. N. (1995). *Basic Econometrics.* McGraw-Hill Inc.

Guner, B. A., Malmendie, U., and Tate, G. (2005). The Impact of Boards with Financial Expertise on Corporate Policies. *Journal* , 1-63.

Han, K. C., and Suk, D. Y. (1998). The Effect of Ownership Structon. *Review of Financial Economics , 7* (2), 143-15.

Hutchinson, M., and Zain, M. M. (2009). Internal Audit Quality, Audit Committee Independence, Growth Opportunities and Firm Performance. *Internal audit quality, audit committee independence, growth opportunities and firm performance , 7* (2), 50-63.

Jensen, M. C., and Meckling, W. (1976). Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Sructure. *Journal of Financial Economics* , 305-360.

Johnson, S., Boone, P., and Breach, F. E. (2000). Corporate Governance in Asian Financial Crisis. *Journal of Financial Economics , 58*, 141-186.

Kamardin, H., and Haron, H. (2011). Internal corporate governance and board performance in monitoring roles Evidence from Malaysia. *Journal of Financial Reporting , 9* (2), 119-140.

Kie, G. C., and Nicholson, G. J. (2003). Boar Composition and Corporate Governance. *Corporate Governanc: Internationa Review , 11* (3), 189-205.

Kim, H. s., and Lim, C. (2010). Diversity, outside directors andfirm valuation: Korean evidence. *Journal of Business Research , 63*, 284-291.

Klein, A. (2002). Economic Determinants of Audit Committee Independence. *Ameican Accounting Association , 77* (2), 435-452.

Leng, A. C. (2004). The Impact of Corporate Governance Practices on Firms' Financial Performance. *ASEAN Economic Bulletin , 21* (3), 308-18.

Liew, P. K. (2007). Coporate Governance Performance: Key Players. *Corporate Governance , 5* (15), 724-741.

Madura. (2010). *International Corporate Finance.* China : China Translation & Printing Services Limited.

Mark, Y. T., and Kusmadi, Y. (2005). Size Realy Matters: Further Evidence on the Negatie Relatioship between Board Size and Firm Value. *PACIFIC-BASIN FINANCE JOURNAL , 13*, 301-318.

Maury, B. (2006). Family ownership and firm performanc e: Empirical evidence from Western European corporations. *Journal of Corporate Finance , 12*, 321-341.

McConaughy, D. L., Matthews, C. H., and Fialko, A. S. (2001). Founding Family Controlled Firms: Performance, Risk, and Value. *Journal of Small Business Management , 39* (1), 31-49.

Nasir, K., Al-Khatib, K., & Khabhari, Y. (2002). Emperical evidence on the depth of corporate information disclosure in developing countries: The case of Jordan. *International Journal of Commerce and Managerial , 12* (3/4), 122-155.

O'Boyle Jr., E. H., Pollack, J. M., and Rutherford, M. W. (2012). Exploring the relation between family involvement and firms' financial performance: A meta-analysis of main and moderator effects. *Journal of Business Venturing , 27*, 1-18.

O'Connell, V., and Cramer, N. (2010). The relationship between firm performance and board characteristics in Ireland. *European Management Journal , 28*, 387-399.

Padilla, A. (2002). Can Agency Theory Justify The Regulation Of Insider Trading. *The Quarterly Journal of Austrian Economics , 5* (1), 3-38.

Ponnu, C. H., and Karthigeyan, R. M. (2010). Board independence and corporate performance: Evidence from Malaysia. *African Journal of Business Management , 4* (6), 858-868.

Saito, T. (2008). Family firms and firm performance: Evidence from Japan. *Journal of The Japanese and International Economies , 22*, 620-646.

Sama, L., & Shoaf, V. (2005). Reconciling Rules and principles: An Ethical Based Approach to Corporate Governance. *Journal of Business Ethics* , 58, 177-185.

Shamsher, M., Zulkarnain, M. S., and A-Ali, A. H. (2001). compliance Audit Committee: A brief review of the practice. *Akauntan Nasional: Journal of Malaysian Institute of Accounting , 14*, 4-7.

Sori, Z. M. and Ramdili, S. M. (2009). Audit Committee and Auditor Independence: The Bankers' Perception. *Journal of Economics and Management , 3* (2), 317-331.

Stewart, J., and Munro, L. (2007). The Impact of Audit Committee Existence and Audit Committee Meeting Frequency on the External Audit: Perceptions of Australian Audit: Perceptions of Australian Auditors. *International Journal of Auditing , 11*, 51-69.

Welch, E. (2003). Institutional ownership and firm perfomance. *Australian Journal of Management , 28* (3), 19-38.

Yasser, Q. R. (2011). Corporate governance and performance: An Analysis of Pakistani listed firms. *International Research Journal of Library, Information and Archival Studies , 1* (3), 81-90.

Yermack, D. (1996). Higher Market Evaluation of Companies with a Small Board of Directos. *Journal of Financial Economics , 40*, 185-211.

Young, C.-S., Tsai, L.-C., and Hsieh, P.-G. (2008). Voluntary Appointment of Independent Directors in Taiwan: Motives and Consequences. *Journal of Business Finance , 35* (9), 1103-1137.

Zhang, Y., Zhou, J., and Zhou, N. (2007). Audit committee quality, auditor independence, and internal control weaknesses. *Journal of Accounting and Public Policy , 26*, 300-327.