

**CORPORATE GOVERNANCE AND PERFORMANCE OF
NON-FINANCIAL PUBLIC LISTED FIRMS IN OMAN**

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PUBLIC LISTED FIRMS IN OMAN**

By

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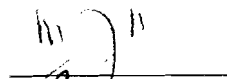
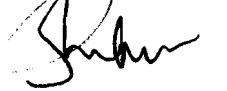

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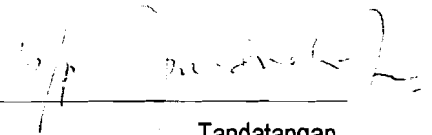
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ABSTRACT

Corporate governance issues have been having the share of attention from researchers for over three decades owing to the increasing of global economic crisis. Hence, this study attempts to contribute to literature by investigating such relationship in Oman, a developing country. Specifically, this study investigates the relationship between the corporate governance mechanisms (board of director's characteristics, the audit committee characteristics, and the executive committee) and the performance of listed companies in Oman for the year 2008 to 2012. The model of this study was theoretically founded on both the agency and the resource dependence theories. To examine the developed model, the required data were gathered from the annual reports of 78 non-financial listed firms. In analysing the data, this study utilised the panel data methodology on 78 companies with 390 observations. Moreover, this study used firm size, leverage, industry and years as control variables. Based on the panel data results, the random effect model was used to examine the effect of the predictors on the firm performance measured by Return on Assets (ROA) and Tobin's Q. The statistical results show that board size, board meeting and time period (2010) were a positive determinant of Tobin's Q while audit committee meeting and executive committee existence were negative determinants of Tobin's Q. On the other hand, the secretary role, leverage and time period (2011) were negative predictors of ROA. From the practical and the theoretical contribution points of view, this study indicate that the resource dependence theory is more significant compared to the agency theory when describing corporate governance practices in Oman. Besides providing suggestions for future research work, this study provides several recommendations for regulators (the Capital Market) and Omani companies.

Keywords: corporate governance, firm performance, board of directors characteristics, audit committee characteristics, executive committee existence, Oman

ABSTRAK

Isu tadbir urus korporat telah mendapat perhatian penyelidik selama lebih daripada tiga dekad berikutan peningkatan krisis ekonomi global. Oleh itu, kajian ini bertujuan untuk menyumbang kepada literatur dengan menyiasat hubungan tersebut di Oman, sebuah negara yang membangun. Secara khusus, kajian ini menyelidik hubungan antara mekanisme tadbir urus korporat (ciri-ciri lembaga pengarah, ciri-ciri jawatankuasa audit, dan jawatankuasa eksekutif) dan prestasi syarikat-syarikat yang disenaraikan di Oman bagi tahun 2008 hingga 2012. Model kajian ini secara asasnya dibina berdasarkan teori agensi dan teori pergantungan sumber. Untuk mengkaji model yang dibangunkan, data yang diperlukan telah dikumpul daripada laporan tahunan 78 buah firma bukan kewangan yang disenaraikan. Dalam menganalisis data, kajian ini menggunakan kaedah data panel dari 78 buah syarikat dengan menjalankan 390 pemerhatian. Selain itu, kajian ini menggunakan saiz firma, keumpulan (*leverage*), industri dan tahun sebagai pembolehubah kawalan. Berdasarkan keputusan data panel, model kesan rawak telah dipilih sebagai cara untuk mengkaji kesan ramalan prestasi firma yang diukur melalui pulangan aset (ROA) dan juga Tobin Q. Keputusan statistik menunjukkan bahawa saiz lembaga pengarah, mesyuarat lembaga pengarah dan tempoh masa (2010) adalah penentu positif Tobin Q, manakala kewujudan mesyuarat jawatankuasa audit dan jawatankuasa eksekutif adalah penentu negatif Tobin Q. Sebaliknya, peranan setiausaha, keumpulan (*leverage*) dan tempoh masa (2011) adalah peramal negatif ROA. Dari sudut praktikal dan teori, kajian ini menunjukkan bahawa teori pergantungan sumber adalah lebih penting berbanding dengan teori agensi apabila memerihalkan amalan tadbir urus korporat di Oman. Selain menyediakan cadangan untuk kerja-kerja penyelidikan pada masa hadapan, kajian ini memberikan beberapa cadangan bagi pengawal selia (Pasaran Modal) dan syarikat-syarikat di Oman.

Kata kunci: tadbir urus korporat, prestasi firma, ciri-ciri lembaga pengarah, ciri-ciri jawatankuasa audit, kewujudan jawatankuasa eksekutif, Oman

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TABLE OF CONTENT

TITLE	PAGE
TITLE PAGE	i
CERTIFICATION OF THESIS WORK	ii
PERMISSION TO USE	iv
ABSTRACT	v
ABSTRAK	vi
ACKNOWLEDGEMENTS	vii
TABLE OF CONTENT	ix
LIST OF TABLES	xxiii
LIST OF FIGURES	xxv
LIST OF ABBREVIATIONS	xxvi
LIST OF APPENDICES	xxxi
CHAPTER ONE	1
INTRODUCTION	1
1.1 Background of the Study	1
1.2 Problem Statement	17

1.3 Research Questions	25
1.4 Research Objectives	26
1.5 Significance of the Study	26
1.5.1 Theoretical Significance	27
1.5.2 Practical Significance	30
1.5.3 Policy Making Significance	31
1.6 Definition of Terms	31
1.6.1 Firm Performance	31
1.6.2 Corporate Governance Mechanisms	32
1.6.2.1 Board of Director's Characteristics	32
1.6.2.1.1 Board Size	32
1.6.2.1.2 Board Independence	32
1.6.2.1.3 Board Meeting	32
1.6.2.1.4 Board Change	33
1.6.2.1.5 The Role of the Secretary of the Board	33
1.6.2.1.6 Legal Counsel	33
1.6.2.1.7 Foreign Member on the Board	33

1.6.2.2 Audit Committee Characteristics	33
1.6.2.2.1 Audit Committee Size	33
1.6.2.2.2 Audit Committee Independence	34
1.6.2.2.3 The Audit Committee Meeting	34
1.6.2.3 The Executive Committee Existence	34
1.6.3 Control Variables	35
1.6.3.1 Firm Size	35
1.6.3.2 Leverage	35
1.6.3.3 Industry	35
1.6.3.4 Time Period	35
1.7 Scope of the Study	35
1.8 Organisation of the Study	37
CHAPTER TWO	39
BACKGROUND OF OMAN	39
2.1 Introduction	39
2.2 Background of Oman	39
2.2.1 Economic View	41

2.2.1.1 Overview of Macroeconomic	42
2.2.1.1.1 Economy Growth	42
2.2.1.1.2 Foreign Direct Investment (FDI)	43
2.2.1.1.3 Inflation	44
2.2.1.1.4 Financial Situation	45
2.2.1.1.5 Currency	45
2.2.1.1.6 External Account	46
2.3 Economic Brief in Gulf Cooperation Council (GCC) States	46
2.4 Corporate Governance in Emerging Markets	48
2.5 Performances in Gulf Cooperation Council Market	49
2.6 Corporate Governance in Oman	50
2.7 Summary of the Chapter	57
CHAPTER THREE	58
LITERATURE REVIEW	58
3.1 Introduction	58
3.2 Firm Performance	58
3.2.1 The Firm Performance Definition and Measurement	58

3.2.2 The Importance of Performance	62
3.3 Corporate Governance	63
3.3.1 Corporate Governance Definitions	63
3.3.2 Corporate Governance Importance	67
3.4 Corporate Governance and Firm Performance	73
3.5 Board of Directors Characteristics and Firm Performance	79
3.5.1 Board Size and Firm Performance	80
3.5.2 Board Independence and Firm Performance	89
3.5.3 Board Meeting and Firm Performance	98
3.5.4 Board Change and Firm Performance	102
3.5.5 The Role of the Secretary on the Board and Firm Performance	106
3.5.6 The Legal Counsel and Firm Performance	109
3.5.7 Foreign Member on the Board and Firm Performance	111
3.6 Audit Committee Characteristics and Firm Performance	115
3.6.1 Audit Committee Size and Firm Performance	115
3.6.2 Audit Committee Independence and Firm Performance	123
3.6.3 Audit Committee Meeting and Firm Performance	125

3.7 The Executive Committee and Firm Performance	129
3.8 Underpinning Theories	135
3.8.1 Agency Theory	135
3.8.2 The Resource Dependence Theory	139
3.9 Summary of the Chapter	142
CHAPTER FOUR	143
RESEARCH FRAMEWORK AND HYPOTHESES DEVELOPMENT	143
4.1 Introduction	143
4.2 Theoretical Framework	143
4.3 Hypotheses Development	147
4.3.1 Firm Performance	148
4.3.1.1 ROA	148
4.3.1.2 Tobin-Q	149
4.3.2 The Board of the Directors Characteristics and Firm Performance	152
4.3.2.1 The Board Size and Firm Performance	152
4.3.2.2 Board Independence and Firm Performance	156
4.3.2.3 Board Meeting and Firm Performance	161

4.3.2.4 Board Change and Firm Performance	164
4.3.2.5 The Role of Secretary on the Board and Firm Performance	166
4.3.2.6 The Legal Counsel and Firm Performance	168
4.3.2.7 Foreign Member on the Board and Firm Performance	170
4.3.3 Audit Committee Characteristics and Firm Performance	172
4.3.3.1. Audit Committee Size and Firm Performance	173
4.3.3.2 Audit Committee Independence and Firm Performance	175
4.3.3.3 Audit Committee Meeting and Firm Performance	177
4.3.4 The Executive Committee and Firm Performance	179
4.3.4.1 The Executive Committee Existence and Firm Performance	182
4.4 Control Variables	184
4.4.1 Firm Size	184
4.4.2 Leverage	185
4.4.3 Industry	186
4.4.4 Time Period	188
4.5 Summary of the Chapter	189
CHAPTER FIVE	190

RESEARCH METHODOLOGY	190
5.1 Introduction	190
5.2 Research Design	190
5.3 Panel data	191
5.4 Data Collection Procedures	194
5.4.1 Population and Sample	194
5.5 Unit of Analysis	198
5.6 Model Specification and Multivariate Regressions	198
5.7 Measurement of the Variables	201
5.8 Proposed Panel Data Analysis Technique	205
5.8.1 Descriptive Analysis	205
5.8.2 Correlation of Variables	205
5.8.3 Diagnostic Tests	205
5.8.3.1 Normality	206
5.8.3.2 Outliers	207
5.8.3.3 Multicollinearity	207
5.8.3.4 Contemporaneous Correlation	208

5.8.3.5 Heteroskedasticity	208
5.8.3.6 Autocorrelation	209
5.9 Data Analysis and Interpretation	210
5.9.1 Getting Data Analysis-Ready	210
5.9.2 Panel Data Analysis	211
5.9.2.1 Fixed Effects Model	212
5.9.2.2 Random Effects Model	213
5.10 Multivariate Regression Analysis	214
5.11 Summary of the Chapter	214
CHAPTER SIX	215
ANALYSIS AND FINDING	215
6.1 Introduction	215
6.2 Analysis of the Sample	215
6.3 Companies Profile	216
6.4 Descriptive Statistics	219
6.5 Correlation Analysis	227
6.6 Panel Data Analysis	231

6.6.1 Outlier Detecting	232
6.6.2 Diagnostic Tests	233
6.6.2.1 Normality	234
6.6.2.2 Checking the Multicollinearity	235
6.6.2.3 Checking of Linearity	237
6.6.2.4 Checking of Heteroscedasticity	237
6.6.2.5 Checking of Contemporaneous Correlation	239
6.6.2.6 Checking of Autocorrelation	240
6.7 Results of LM Test	242
6.8 Results of F Test	243
6.9 Results of Hausman Test	244
6.10 GLS estimation	246
6.11 Model Estimation	248
6.12 Evaluation of the Models	248
6.12.1 Model 1 (ROA as Dependent Variable)	249
6.12.2 Model 2 (Dependent Variable Tobin-Q)	254
6.13 Hypotheses Testing	257

6.13.1 Model (1) and Result of Analysis	257
6.13.1.1 Control Variables and ROA	258
6.13.1.2. Board of Director’s Characteristics and ROA	260
6.13.1.3 Audit Committee Characteristics and ROA	261
6.13.1.4 Executive Committee and ROA	261
6.13.2 Model (2) and Result of Analysis	262
6.13.2.1 Control Variables and Tobin-Q	263
6.13.2.2 Relationship between Board of Directors’ Characteristics, Audit Committee Characteristics, Executive Committee and Tobin-Q	265
6.13.2.2.1 Board of Director’s Characteristics and Tobin-Q	265
6.13.2.2.2 Audit Committee Characteristics and Tobin-Q	266
6.8.2.2.3 Executive Committee and Tobin-Q	266
6.14 Summary of Hypotheses Testing: Corporate Governance and Firm Performance	267
6.16 Summary of the Chapter	270
CHAPTER SEVEN	271
DISCUSSION AND CONCLUSION	271
7.1 Introduction	271
7.2 Summary of the Study	271

7.3 Discussion of Hypotheses	279
7.3.1 Discussion of First Model (Results Based on Accounting Measure)	280
7.3.1.1 Board of Director's Characteristics	280
7.3.1.1.1 Board Size and ROA	280
7.3.1.1.2 Board Independence and ROA	283
7.3.1.1.3 Board Meeting and ROA	286
7.3.1.1.4 Board Change and ROA	288
7.3.1.1.5 The Role of the Secretary on the Board and ROA	289
7.3.1.1.6 Legal Counsel and ROA	290
7.3.1.1.7 Foreign Member on the Board and ROA	291
7.3.1.2 Audit Committee Characteristics	292
7.3.1.2.1 Audit Committee Size and ROA	292
7.3.1.2.2 Audit Committee Independence and ROA	294
7.3.1.2.3 Audit Committee Meeting and ROA	296
7.3.1.3 Executive Committee and ROA	297
7.3.2 Discussion of Second Model (Results Based on Marketing Measure)	298
7.3.2.1 Board of the Director's Characteristics	299

7.3.2.1.1 Board Size and Tobin-Q	299
7.3.2.1.2 Board Independence and Tobin-Q	300
7.3.2.1.3 Board Meeting and Tobin-Q	302
7.3.2.1.4 Board Change and Tobin-Q	303
7.3.2.1.5 The Role of Secretary on the Board and Tobin-Q	304
7.3.2.1.6 Legal Counsel and Tobin-Q	305
7.3.2.1.6 Foreign Member on the Board and Tobin-Q	306
7.3.2.2 Audit Committee Characteristics	307
7.3.2.2.1 Audit Committee Size and Tobin-Q	307
7.3.2.2.2 Audit Committee Independence and Tobin-Q	308
7.3.2.2.3 Audit Committee Meeting and Tobin-Q	310
7.2.2.3 Executive Committee Existence and Tobin-Q	311
7.4 Implications of the Study	312
7.4.2 Implications to Practice	320
7.4.3 Implications to Policy Makers	323
7.5 Limitations of the Study and Suggestions for Future Research	324
7.6 Conclusion of the Study	327

REFERENCES

329

APPENDICES

386

LIST OF TABLES

Table	Page
1.1 Indicators of Poor Performance	22
1.2 The Scope Of Study	36
5.1 Sample of Study	195
5.2 Summary of Variables Measurement	202
6.1 Analysis of the Sample	216
6.2 Frequency of the Companies Regarding to the Board Change Variable	217
6.3 Frequency of the Companies Regarding to the Secretary Variable	217
6.4 Frequency of the Companies Regarding to the Legal Counsel Variable	218
6.5 Frequency of the Companies Regarding to Executive Committee Existence Variable	218
6.6 Frequency of the Companies Regarding to Industry Variable	219
6.7 Descriptive Statistics of Continuous Variables	219
6.8 Results of Pearson Correlation Analysis	230
6.9 Multicollinearity Test	236
6.10 The Standard Deviation of Firm Performance and the Residuals	237
6.11 Breusch-Pagan/Cook-Weisberg Test	239
6.12 Pesaran's Test	240
6.13 Wooldridge Test	241
6.14 Durbin-Watson Test	242
6.15 LM Test	243

6.16	F Test	244
6.17	Hausman Test	246
6.18	Regression Results of Model 1 (Dependent= ROA)	253
6.19	Regression Results of Model 2 (Dependent= Tobin-Q)	256
6.20	Summary of the Hypotheses Related to ROA	262
6.21	Summary of the Hypotheses Related to Tobin-Q	267
6.22	Summary of the Hypotheses Testing Results	269
7.1	Summary of The All Findings	279

LIST OF FIGURES

Figure		Page
1.1	The Role of Corporate Governance in Reducing the Problem of Conflict of Interest	4
1.2	The dimensions of corporate governance	13
1.3	The Performances in GCC Market	19
1.4	The Price Performance Index in Oman	20
2.1	The Performances in GCC Market	49
3.1	The Good Application Properties for Corporate Governance	73
4.1	Research Framework	147

LIST OF ABBREVIATIONS

ACC	:	Audit Committee Characteristics
ACINDE	:	The Audit Committee Independence
ACMEETIN	:	The Audit Committee Meeting
ACSIZE	:	The Audit Committee Size
BD	:	Board Diversity
BOARDCH	:	The Board Changes
BOARDME	:	The Board Meeting
BOARDSIZE	:	The Board Size
BOD	:	Board of Director
BOFOREIGN	:	The Foreign Member on the Board
BORADINDE	:	The Board Independence
BRC	:	Blue Ribbon Committee
CARs	:	Superior to Cumulative Abnormal Returns
CCL		Commercial Companies Law
CEO	:	Chief Executive Officer
CG	:	Corporate Governance

CMA	:	Capital Market Authority
COC	:	Cost of Capital
CTA	:	Cash to Assets
DY	:	Dividend Yield
ECEX	:	Executive Committee Existence
EPS	:	Earnings per Share
ETA	:	Expense to Assets
ETS	:	Expenses to Sale
FCI	:	Foreign Capital Investment
FDI	:	Foreign Direct Investment
FIRMSIZE	:	Firm Size
FP	:	Firm Performance
GCC	:	Gulf Cooperation Council
GRO	:	Growth in Sales
IMF	:	International Monetary Fund
INDUSTRY	:	Industry
KPMG		Klynveld Peat Marwick Goerdeler

LEGALCO	:	The Legal Counsel
LEVERAG	:	Leverage
LMC	:	Log of Market Capitalization
LP	:	Labour Productivity
MCI		Modern Cold Industrialisation
MSM	:	Muscat Securities Market
MSM		Muscat Securities Market
MTBV	:	Market-to-Book Value
MVA	:	Market Value Added
NEDs		Non-Executive Directors
OCF	:	Operating Cash Flow
OCM		Oman Capital Market
OECD	:	Organization for Economic Co-operation and Development
OMR	:	Omani Rial
OP	:	Operation Profit
OPEC	:	Organisation of Petroleum Exporting Countries
OSC	:	Omani Security Commission

PAIPED	:	Public Authority for Investment Promotion and Export Development
PAIPED	:	Public Authority for Investment Promotion and Export Development
PE	:	Price-Earnings Ratio
PM	:	Profit Margin
PPE	:	Profit per Employee
RET	:	Abnormal Returns; Annual stock return
ROA	:	Return on Assets
ROA	:	Return on Assets
ROCE	:	Return on Capital Employed
ROE	:	Return on Equity
ROFA	:	Return on Fixed Assets
ROI	:	Return on Investment
ROR	:	Return on Revenue
ROS	:	Return on Sales
SEC	:	Securities and Exchange Commission
SECRETA	:	The Secretary Role on the Board
SOA	:	Sarbanes Oxley Act

SR	:	Stock Repurchases
STS	:	Sales to Assets
TIMEPER	:	The Time Period
TOBINSQ	:	Tobin-Q Ratio
UAE	:	United Arab Emirates
UK	:	United Kingdom
UNDP	:	United Nations Development Program
US	:	United State
USD	:	United State Dollar
WTO	:	World Trade Organization

LIST OF APPENDICES

Appendix		Page
Appendix A	TABLES OF PREVIOUS LITERATURE REVIEW	388
Appendix B	OMANI CODE OF CORPORATE GOVERNANCE	422
Appendix C	OUTCOME FOR ANALYSIS	439
Appendix D	MUSCAT STOCK MARKET -NON-FINANCIAL COMPANIES LIST	445

CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

Businesses all over the world are in need of development and growth in the quest to acquire investments. Prior to invest in a specific business, investors often ensure that the business is financially secure and stable and it is able to generate profits in the long term (Al Manaseer, Al-Hindawi, Al-Dahiyat & Sartawi, 2012; Khan, Nemati & Iftikhar, 2011; Mallin, 2007). Therefore, in cases where the company's position is adverse, the stakeholders are less interested to invest. This incompetence to attract enough investment often results in adverse results for the business industry and the country's economy.

With the advent of the Asian financial crisis in 1997, 1998 and the recent crisis involving Enron, WorldCom and Ahold among others, in Europe and America, confidence on corporate institutions, legislative bodies and agencies is all-time low. The primary problem highlighted during the crisis was acquiring a significant amount of short-term debts by the operations and transactions in-house staff, relatives and friends involved in the businesses, government and companies. These debts are practiced to be concealed through different accounting methods and the systems of innovation. In response to the collapse of some leading companies such as Enron, WorldCom and Ahold, thorough investigations had been conducted and one of the main reasons behind that disaster identified was the manipulation of their financial statements. Hence, a great attention has

been given to corporate governance to provide a mechanism that protects investors by ensuring proper management practices (Bøhren & Strøm, 2010; Brown & Caylor, 2006; Jackling & Johl, 2009; Khanchel, 2007; Mokhtar *et al.*, 2009).

Corporate governance, as a mechanism, has been one of the topics of interest to many researchers to reduce the conflicts of interest between management and the investors. This mechanism aims to protect the owners of capital from opportunistic dispositions (Abdurrouf, 2011; Jensen & Meckling, 1976; Pandya, 2011; Pfeffer, 1972; Shleifer & Vishny, 1986) and to ensure that managers perform their best to achieve the interests of the shareholder and stakeholders. Therefore, corporate governance mechanisms and regulations have been given a considerable attention worldwide as, they enhance the overall economic proficiency to achieve the overall public benefits of the individual and organisational stakeholders (Bozec, 2005; Hsu & Petchsakulwong, 2010; Saibaba & Ansari, 2011). Significantly, both local and foreign investors will be substantially attracted to the companies where the corporate governance mechanisms are being in practice. The proper execution of the Corporate Governance Code can prevent not only the financial disputes, but can reduce the corruption as well, thus enhancing the overall firm growth that collectively contributes in stimulating the country's overall economic growth and development (Al-Matari, Al-Swidi, Faudziah, Al-Matari, 2012a).

The issue of corporate governance has become one of the most prevalent and communal subjects in the business environment regarding investment in Gulf countries. It has gained substantial importance because of the following factors: enormous developments,

its significance in the practices of the departments of companies, dealing with shareholders and the manner and method of preserving the rights of shareholders. Finally, it led to various financial collapses and administrative major international companies, and the prevalence of financial and administrative corruption, which led to the collapse of major economies of the countries in the last decade (Al Manaseer *et al.*, 2012).

Corporate governance has become a major concern in both corporate and academic worlds. This consternation in the business world emanates from the perceived importance of moral and ethical conduct in business, which creates general climate (environment, both legal and social) promoting good corporate governance. While in academia, it has been determined that business decisions are never made in a vacuum. Business decision makers have goals other than business objectives. For instance, managers are interested about their personal satisfaction rather than their employees, as well as benefits of the community (society) in general. These objectives negatively influence the equity (Fama & Jensen, 1983; Sheifer & Vishny, 1997). The structures of corporate governance stipulate the distribution of rights and responsibilities among various stakeholders in a society, as the board directors, shareholders, etc. and clarify the rules and procedures for making decisions on corporate matters. This is consistent with the view of Obiyo and Lenee (2011).

Many researchers, organisations and institutions agree that the role of corporate governance reduces the problem of conflict of interest as this study often mentions. The

following Figure 1.1 illustrates the role of governance in reducing the problem of conflicts of interest.

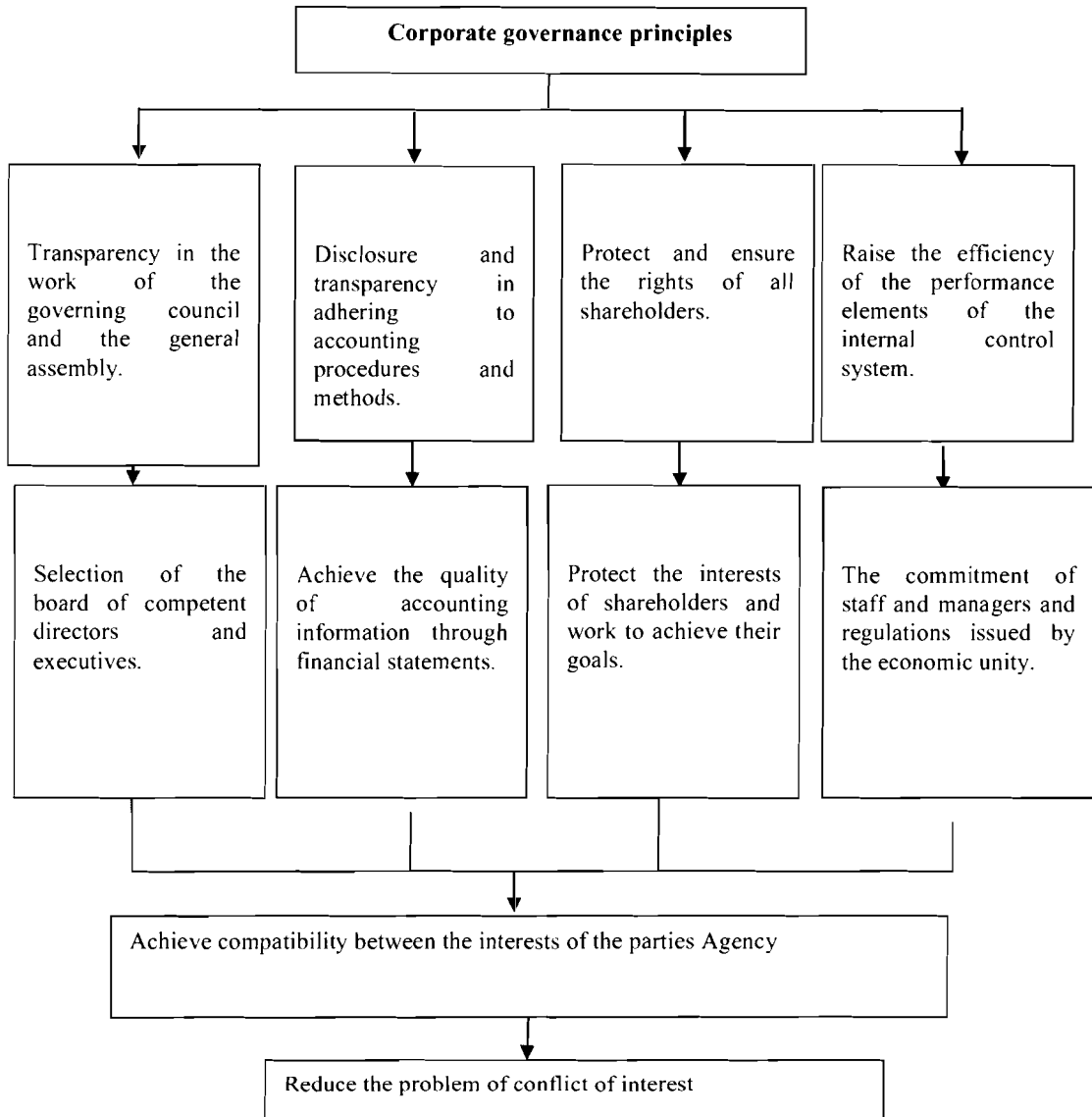


Figure 1.1
The Role of Corporate Governance in Reducing the Problem of Conflict of Interest
 Source: Nuri and Salman (2010)

There are few studies in the Gulf and Arab countries that have focused on the performance of the board of directors and its members, prior to develop corporate governance charter (Mubarak, 2011). This detail is missing, as they failed to emphasise on the qualification of board members, their awareness of principles, policies and the concepts of governance. In addition, it reflects on how to manage companies while being the members of the official board of directors. The members of the board are required to concentrate on the company's performance, safety, financial, administrative, organisational and legal situation. The board members must develop a strategy to minimise conflicts of interests and they should keep themselves away from decision-making, as the existence of conflict of interest would compromise their position and prevent them from sincerely doing their job. The corporate governance charter comprises the board of directors' duties; their selection, appointment and monitoring of the companies' executive heads (Mubarak, 2011).

It has been widely debated that regulations should be established to encourage companies and to abolish poor practices of corporate governance in Gulf countries. Regulators should reform corporate governance urgently in state-owned companies, which are the economics' major contributors of the Gulf Cooperation Council (GCC). The reformation of corporate sector accelerated by acquiring suppliers and private sector companies and to apply the standards of good governance (Ahmed & Abdullah, 2010). Since, these companies are also contributors. By and large, the corporate governance mechanism

should be given more attention by the government and companies to ensure the high performance profile.

In the same way, Al Rashid and Jamal (2010) claimed that corporate governance has increasing significance in GCC countries because of the weak existing legal systems that hinder companies to resolve their disputes and to offer freedom of information transparency. These factors act as a ground of ineffective supervision, extensive corruption and lack of confidence. The primary resolution to the overhead issue is the dissemination of corporate governance rules and principles, which will control corruption and ineffective management consequently, providing transparency in the economic sectors. They stated that corporate governance hinges on private and public sector cooperation in creating a competitive marketplace - a situation that calls for the application of regulations and laws, the adoption of transparency and reforms, and the upgrading of economic prospects' structures that can improve both sectors' competitiveness. It also calls for the development of plans and the application of governance mechanisms in companies and organisations to achieve significant growth rates on a yearly basis.

In the context of emerging markets in general, corporate governance has attained greater importance due to the weak legal system. It may cause several disputes. Additionally, the inauthentic information results in deterring effective supervision and control therefore, encourage the spread of corruption and lack of confidence. On the other hand, applying the doctrines of corporate governance assists in creating the needed precautions against

mismanagement and corruption and encourages transparency in economic life, not to mention eradicating the resistance to reforms in institutions (Baydoun, Ryan & Willett, 2008).

Consequently, international organisations are now very particular concerning issues of governance. For instance, the International Monetary Fund has mandated the improvements of governance and has included this in its debt relief program. In addition, in 1999, the Organisation of Economic Cooperation and Development (OECD) established the influential OECD Principles of corporate governance in an attempt to assist both member and non-member countries to conduct an evaluation and, to enhance the legal, institutional and regulatory framework for effective corporate governance. Moreover, private firms including Standard and Poor (S&P), California Public Employees' Retirement Pension System, Credit Lyonnais Securities Asia (2001) and McKinsey are stressing on significant reforms in governance practices (Khanchel, 2007).

There are several corporate governance charters and instructions issued by the Arab countries, including Oman, Saudi Arabia, Bahrain, Jordan and Egypt; with the majority of the charters concentrating on significant topics concerning, the governing of the shareholders-directors relationship, the directors-management relationships, the transactions of related parties, the election and appointment methods of the board of directors. These also include the experts' presence among the non-executive members and independent members as well as the role of the Board of Director (BOD), the company's restructuring, work ethics, council rewards and top five executives'

remuneration. Furthermore, these set of charters encapsulate the protection of small shareholders' rights and the promotion of governance culture among the general assembly members and the companies' shareholders for the preservation and awareness of the minority shareholders' rights (Mubarak, 2011).

The current CG report emphasised that in the past decade, significant developments are made in the light of awareness and cognizance of having a corporate governance system as a main element in the foundations of development throughout the Middle East and North Africa, but this is just the first step as, more work has to be done (Koldertsova, 2011). Additionally, the governance institute in Dubai published a report on the level of corporate governance in the region in March 2010. The study highlighted that over 56% of the companies in the region do not have sufficient experience when it comes to corporate governance definitions and benefits and almost 95% of them revealed that the corporate governance practices need improvement in certain aspects. Specifically, the companies called for the improvement of the structures and board of directors' roles and the certain control elements including risk management and internal audit (OECD, 2010).

Several regulatory reporting of the Gulf region's governments highlighted the current global financial crisis that has an impact on the world economies including the Gulf region. They highlighted that the Gulf companies' lack of commitment to the corporate governance principles, the board departments, executive committees' lack of qualification and narrow mindedness resulted in failure of systems and internal control. Ignoring the principles of corporate governance, the inability to conduct follow-ups on

risk assessment and irregularities in financial and administrative departments culminated in the loss of confidence of clients upon these departments (Baydoun, Ryan & Willett, 2010). Therefore, on account of the above scenario, policy makers have to decide upon the launching of a comprehensive set of measures to strengthen the banking and financial sectors, governance framework and the coordination between the regulators and heads of the sectors.

Certainly, the consensus of all the experts, analysts, auditors and corporate studies indicate that the application of the principles of corporate governance works to reduce risks and financial meltdowns and in the same way, work to achieve stability of money market armed with mechanisms, policies, charters and governance principles to avoid the financial crises. The stability of the companies and investment banks in the financial markets also plays a vital role in avoiding and reducing the incidences of manipulation, financial and administrative corruption (Al Manaseer *et al.*, 2012; Kota & Tomar, 2010; Millet-Reyes & Zhao, 2010; Uadiale, .2010)

In the specific context of Oman, the practices of corporate governance is reported to be weak and lacking in transparency of quality accounting, which ended up in the country's financial crisis (Adnan, 2009). The CG significance is evidenced by Razan (2007), who claimed that effective corporate governance often results in the enhancement in the performance of the company and its attractiveness to foreign investors, which have been observed as less improved in the recent years. Moreover, Haddad (2008) added to the argument claiming that the collapse of many economic units initiates from the investors'

loss of confidence in the financial system. Therefore, a new system in the form of CG is the most suitable solution for the issues as evidenced by several researchers, economists, authors and analysts.

Along the same line, Oman is still unfamiliar to incentive plans that have their basis on the company's performance. Therefore, different mechanism, need to be developed for the evaluation of the environment. In a related study, Khalil (2005) revealed that because of the incorrect financial reporting, the Omani Code of Corporate Governance requires improvement in order to reinforce the confidence of the investors in the existing accounting system. This issue in Oman is widely related to the current breakdown of economic units, which led to the loss of stakeholders along with possible investors. This magnifies the need for the CG implementation to resolve the issues and hence leading to the worldwide popularity of the subject in the field of research (Basmah, 2008).

The increasing developments in the Omani business environment and new policies is being implemented are all geared for foreign investment attraction to the country, which is another challenge to the companies therein. It is important that Omani companies should be prepared to tackle these challenges in a manner that will guarantee the enhancement of their financial performance (Ahmed & Abdullah, 2010). Moreover, companies in Oman should adopt good corporate governance mechanisms to make sure that local and foreign investors are attracted because of the transparency.

It is evident that the government, in terms of increasing role of the private sector, has a core position in the Oman marketplace. As governance eventually results in increased confidence in the national economy, a significant role in the capital market, a heightening in the market's capacity to mobilize savings and greater levels of investment, and the reinforcement of the minority shareholders/investors' rights. Along the same intent, the private sector has been showing inclinations to employ corporate governance mechanisms to enhance their development, competitiveness and to ensure that the funds obtained to generate profits and to create new positions in the company (Alhosini, 2011). In Oman, the stock market, the adoption of corporate governance standards governing the listed companies' operations and regulating the relationship between investors and management has made a criterion for listing (Qattan, 2011).

The board of directors is the foremost internal governance mechanism responsible for monitoring executive decisions (Al Manaseer *et al.*, 2012). Likewise, the board has also core position in corporate governance mechanisms and is considered as the main mechanism that shareholders can implement to control top management (John & Senbet, 1998). Additionally, the board is accountable for determining the overall strategy of the firm, and to make sure that sufficient measures exist for the protection of the shareholder value (Keenan, 2004). For that, this study attempts to contribute to substantial variables to the board of director's characteristics such as, the board change, the role of secretary and legal counsel that may lead to enhance the performance of the company.

Company secretaries are the company's representatives as per legal documents and it is the secretary's responsibility to make sure that the company in conjunction with the directors is conducting operations according to the law. On top of it, secretaries are also responsible for registering the company, communicating with shareholders in distributing dividends. In addition, to make sure that the records are maintained (lists of directors and shareholders, and annual accounts). In several countries, private companies have mandated by law to appoint a person to be the company's secretary, one who is often a senior board member (Zimmerman, 1997).

The role of legal counsel in the firm is very essential to mitigate allegations of judicial nature. The legal counsel are expected to give a firm clearer insight into the future contracts and to solve any problem related to legal gaps. With regard to the agency theory, the separation of the jobs provided the power to make the right decision and it helps in monitoring the firm in terms of evaluation and drawing up of firm report regarding its weaknesses. Furthermore, the legal profession's influence upon the board structure has not been extensively studied, although initiatives have been taken, but the description of board independence and the legal profession's impact on the board structure is still untouched (Rose, 2006).

In a study conducted by Rihawi (2008), three dimensions of corporate governance were indicated: investment dimension, social and law dimension and environmental dimension. Following Figure 1.2 illustrates this:

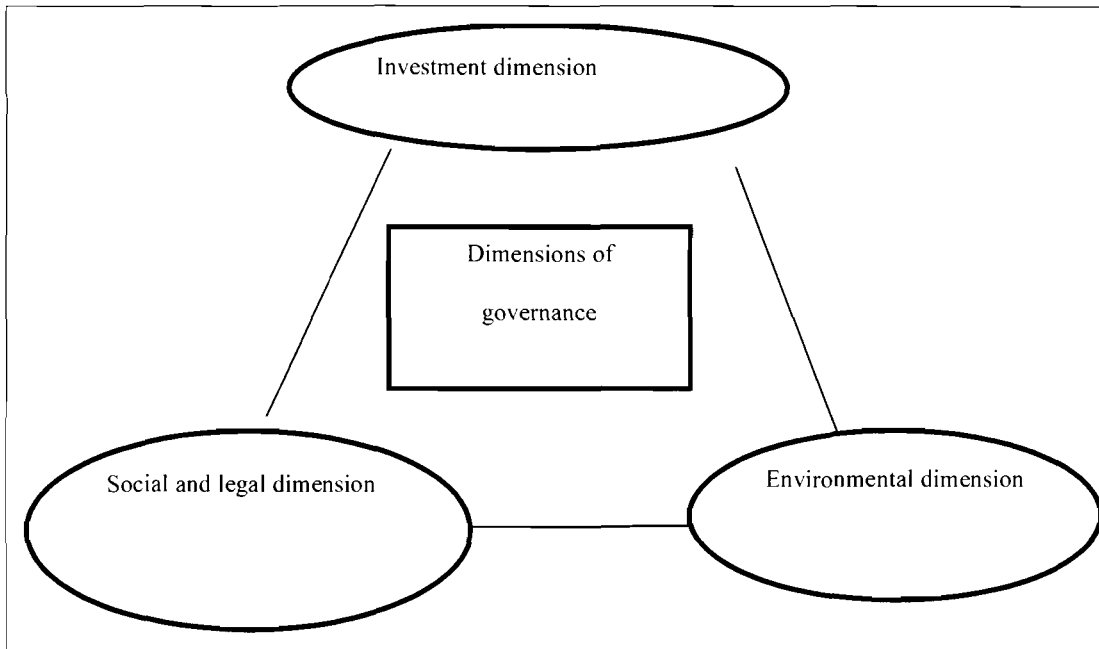


Figure 1.2
The dimensions of corporate governance
Source: Rihawi (2008)

Based on the preceding Figure 1.2 of dimensions of corporate governance, it contends that the social and legal dimension defines the rights and obligations of shareholders and various stakeholders on one hand and of the managers on the other hand and to protect the rights of the minority and small investors. Hence, this study aims to investigate the effect of the legal counsel on the firm performance.

In the light of agency theory, the split-up of two positions in the company can enhance the performance of a firm and increase the wealth of shareholder (Jensen & Meckling, 1976). From other perspective of resource dependence theory, the separation of two

positions in the company may not assist in improving the value of the shareholder (Pfeffer & Slanick, 1979).

The audit committee's role in the implementation of corporate governance principles and in enhancing firm value is significant. According to the principles of corporate governance, audit committees should be independent and carry out their responsibilities with due professional care. In instances of financial manipulation, the audit committee is held accountable for it, which is why the transparency of financial information minimises information asymmetry and enhances firm value (Bhagat & Jefferis, 2002; Heenetigala & Armstrong, 2011).

With the advent of the global financial crisis, which has a bad impact global business entities, the business entities have learnt a great lesson from these negative outcomes, which largely attribute to the inadequate strategies in executive committee. Hence, executive committee has become an important factor in the context of how the company generates profits and maximises shareholder's value while making sure that economic stability is maintained in the country of operation. As reported by economists, the successive crises on the Muscat Securities Market (MSM) have highlighted the weaknesses of governance systems and the public companies' ineffective executive committee. They proposed the importance of creating the competent executive committee, the policy actions and investments diversification to create a strategy of executive committee in every company (Al Rashid & Jamal, 2010). Notwithstanding, the role of executive committee is not even mentioned in the Omani Code of Corporate

Governance though almost all of the listed companies have this committee. Thereupon, this current study expects the executive committee to play a vital role in improving the performance of all listed companies.

In general, effective corporate governance reduces the right of control and authorises managers more power who can take appropriate investment decisions to improve the maximisation of shareholder's wealth. Corporate governance give directors, the rights to make the right decision which services a shareholders' target, whereas at the same time this decision seeks to achieve shareholder and managers goals (Shleifer & Vishny, 1997). This, however, suggests that firms have corporately improved the operating performance (Irina & Nadezhda, 2009). Therefore, this study aims to build a comprehensive model to investigate the factors that can enhance the effectiveness of the corporate governance mechanisms and firm performance in Oman.

This study focuses on Oman (as emerging market) for many significant reasons. Firstly, the majority of the previous studies dedicated to corporate governance and firm performance relationship have confined to developed economies only. It appears that small economies including; Oman is pretty much left out. It has been widely known that there is an inadequacy of studies regarding investigating independence of board of directors. Generally; in the Gulf countries and particularly in Oman firms, responsibilities of the board, sub-committees, the legal system in Oman and their effect on the Omani firms' practices (Al-Hussain & Johnson, 2009; Aljifri & Moustafa, 2007; Al-Matari *et*

al., 2012a; Al-Matari, Al-Swidi, Faudziah, Al-Matari, 2012; Al-Najjar, 2013; Ghabayen, 2012; Najjar, 2012).

Secondly, Muscat Securities Market (MSM) faced an extraordinary crash, which led CMA to the suspension of the trading of two firms, namely, National Rice Mills (SAOG) and Omani National Investment Company Holding (SAOG). These events created a serious question about the efficacy of different monitoring devices that were presumed to protect investors' interests in Oman (Dry, 2003).

Thirdly, the Capital Market Authority (CMA) issued the corporate governance regulations in 2002 in reaction to the Omani corporation management criticism following the 1997 crash. However, the corporate governance in Oman is still in its initial stages and the CMA is attempting to educate the markets on the advantages reaped from effective corporate governance (World Bank, 2009). Additionally, reports assert that several regulations and institutions have just been laid down and are untried, so leading to little awareness of effective corporate governance and moreover these practices are still in their infancy stage.

Fourthly, studies concerning corporate governance in the GCC until now are limited and confined such as Al-Hussain and Johnson (2009) in Saudi Arabia, Aljifri and Moustafa (2007) in the UAE, Al-Matari *et al.* (2012a) and Al-Matari, Al-Swidi, Faudziah, 2012b in Saudi Arabia, Al-Matari *et al.* (2012) in Kuwait, Ghabayen (2012) in Saudi Arabia and Najjar (2012) in Bahrain. Surprisingly, in Oman the relationship between corporate

governance and firm performance has been greatly neglected in the past literature. Likewise, the relationship between the board of directors, audit committee characteristics, executive committee and their effects on firm performance is still deficient in the corporate governance literature. Moreover, the effect of the board diversity as moderator of the relationship between the corporate governance and firm performance is waiting for future examination by future researchers.

Lastly, Oman has been the first country in the Gulf Cooperation Council (GCC) to implement the Code of Corporate Governance back in 2002. Besides, it is the only country in the GCC, which is not a member of the Organisation of Petroleum Exporting Countries (OPEC) and this reason may boost country's economic policies at any time. Subsequently, oil prices in recent years reinforced Oman's budget, trade surpluses, and foreign reserves. Increased expenditures in 2011 associated with Oman's Arab Spring (estimated at RO1 bn, or USD 2.6 bn) offset increased oil revenues while high oil prices helped Oman avoid a budgetary deficit. Therefore, this study attempts to investigate the relationship between corporate governance dimension as mentioned above and their effects on the performance of public listed companies in Oman.

1.2 Problem Statement

In recent years, the diligence on corporate governance has grown exponentially with the major corporate collapses such as Adelphia (2002), Arthur Anderson (2001), Commerce Bank (1991), Enron (2001), Fanny Mae (2008), Freddy Mac (2008), Global Crossing

(2002), Goldman Sachs (2007), Harris Scarfe (2001), HIH (2001), Lehman Brothers (2008), Marconi (2005), Northern Rock (2007), One.Tel (2001), Tyco (2002), WorldCom (2002), Parmalat and Yukos in the US, European and others (Jackling & Johl, 2009; Obiyo & Lenee, 2011; Ii, Kankpang & Okonkwo, 2012).

In the same context of financial crisis, the capital market in the Sultanate of Oman has also experienced its share of corporate dilemmas affecting not only large Omani companies such as National Rice Mills (SAOG) and Oman National Investment Company Holding (SAOG), but several other smaller companies, which had to plead for assistance from the government. The chargers have been cited over the years, revealing that companies hide information and possess incompetent and bungling boards of directors with ineffective and negligent internal controls. In some instances, there have been claims of fraud on the part of directors. Mismanagement of companies and lacklustre board of directors had been blamed for the sharp drop in share prices that occurred in 1998 and the ensuing loss of investor confidence. All of which underscores the need for higher corporate governance standards (Dry, 2003).

In fact, there is a high possibility that the collapse of these two companies is due to the non-application of the principles of corporate governance, which regulates the management of the company and helps to separate the terms of reference and functions. This may also be because of the fact that some companies are under the control of the reigning royalty. Therefore, the collapse of the companies may be attributed to the lack of commitment to the application of the corporate governance.

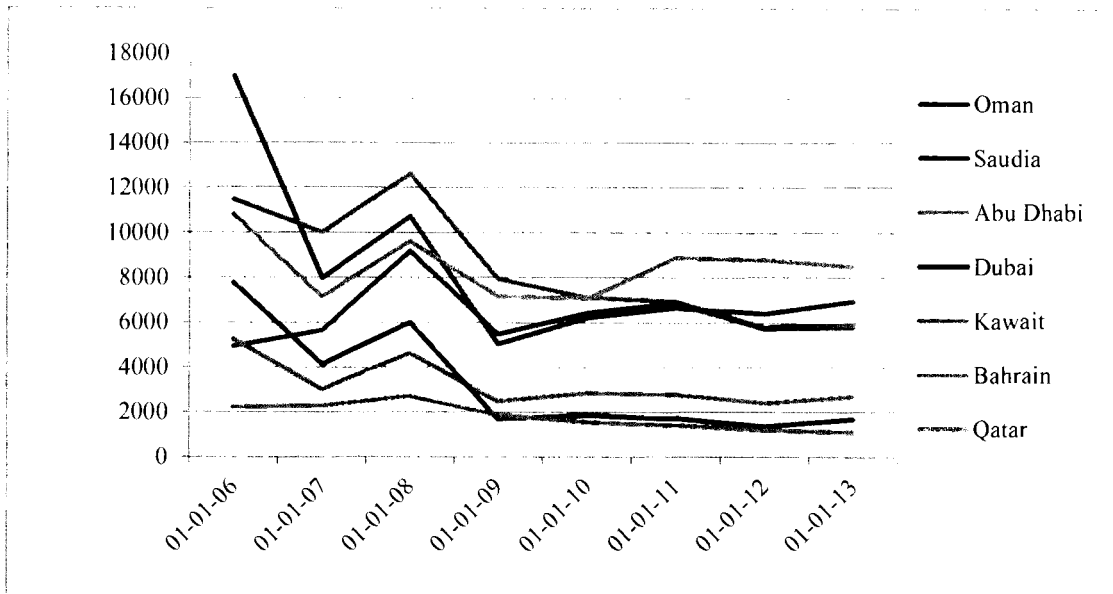


Figure 1.3
The Performances in GCC Market
 Source: GulfBase (2013)

A thorough review of the Gulf markets' performance in the current period reveals that the overall performance experienced fluctuation and significantly declined at the end of year 2009 based on the current available data as depicted in Figure 2.1. Along with the impact of the global financial crisis, this declining and fluctuating trend can be accredited to the lack of capital needs for business expansion and running, owing to the decline of FDI inflows stemming from the investors' lack of confidence in the Gulf companies' corporate governance mechanisms. Stated differently, the ineffective corporate governance mechanisms in the Gulf business environment prevented the improvement of companies' performance. This situation requires more studies to be conducted in the Gulf region to examine the level to which corporate governance could impact the firms' performance in different business sectors.

In the same perspective, several reports and opinions of economic experts confirmed that one of the main causes of the local economic crisis was the susceptibility and lack of corporate governance practices applied by local companies (Al-Matari *et al.*, 2012a). Furthermore, the crisis demonstrated that corporate governance practices applied in the Omani companies have not kept pace with companies competing in global markets. This has contributed directly or indirectly to the increased incidences of faltering companies and shaking investors' confidence, which in turn markedly lead to the negative impact on the market and trading activity.

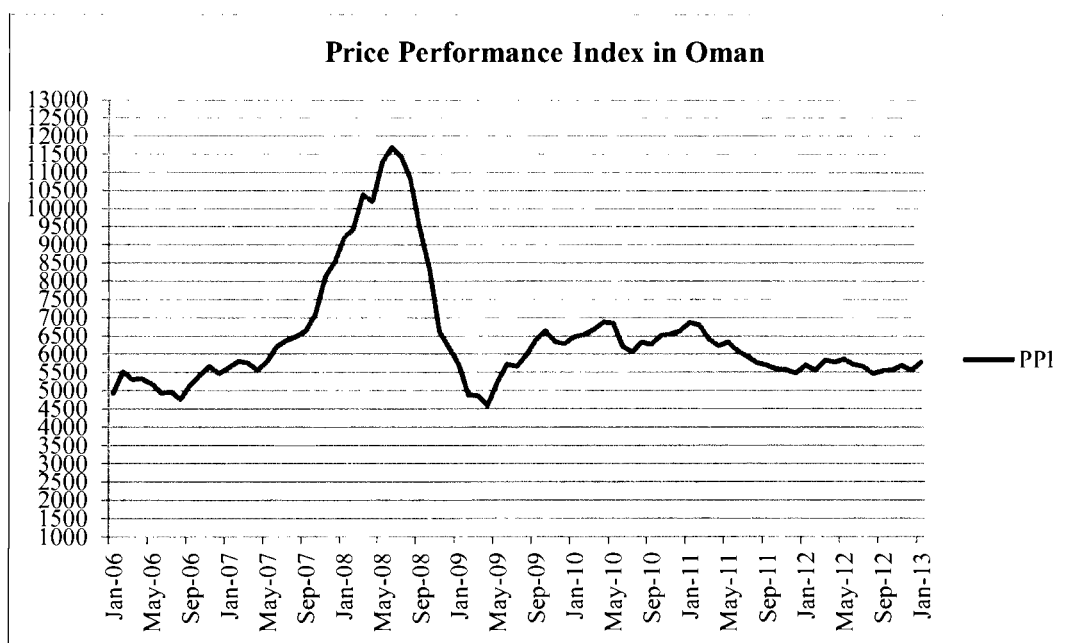


Figure 1.4
The Price Performance Index in Oman
 Source: GulfBase (2013)

Figure 1.4 indicates the declining of the price performance index in Oman. It is clear that in the year 2008, the market index in Oman has drastically decreased. Even though there

was a slight recovery in 2009, the index still decreased during the period from 2009 till 2013. This situation in the Omani market was a major concern for many academics and practitioners. It can be argued that one of the main reasons behind the poor market performance has been the decreasing level of investors' confidence. Due to that, many investors transfer their wealth and profits earned to some other safe, economic and business environment. This lack of confidence was due to the poor implementation of corporate governance mechanisms and the perceived poor protection of the investors (GulfBase, 2013).

Consistent with the conclusion drawn from the graph shown in Figure 1.4, the conclusion was based on the level of Tobin-Q and Return On Assets (ROA). According to the study of Nuryanah and Islam (2011), a higher Tobin's Q with a value greater than 1 suggests a high market value for the company's asset and growth. Moreover, firms have been found to increase their investment opportunities with a Tobin's Q of more than 1, indicating that management has performed well with the assets under its command and have higher growth potential (Eberhart, 2012; Lang & Litzenberger, 1989). However, the percentage of firm performance of the listed companies in Muscat Securities Market (MSM) in 2008, 2009, 2010, 2011 and 2012 as measured by Tobin Q was 27%, 27%, 24%, 36% and 35% respectively indicating the companies' poor performance.

With regards to the ROA, the firm performance is deemed poor if the ROA is negative. In the years 2008, 2009, 2010, 2011 and 2012, 19%, 21%, 21%, 13% and 23% respectively of the listed companies in MSM revealed negative performance based on the Return on

Assets (ROA). This adverse performance has largely blamed many factors (Peng, Buck & Filatotcheve, 2003). It is argued that corporate governance practices were among the factors contributing to the performance of firms (Al-Matari *et al.*, 2012b; Alsaeed, 2006). Similar findings are those of the performance in 2012 is depicted in Table 1.1 as follows;

Table 1.1
Indicators of Poor Performance

Year	ROA	Criterion	Citation	Tobin-Q	Criterion	Citation
2008	19%	-	Peng <i>et al.</i> (2003)	27%	<1	Nuryanah and Islam (2011)
2009	21%	-	Peng <i>et al.</i> (2003)	27%	<1	Nuryanah and Islam (2011)
2010	21%	-	Peng <i>et al.</i> (2003)	24%	<1	Nuryanah and Islam (2011)
2011	13%	-	Peng <i>et al.</i> (2003)	36%	<1	Nuryanah and Islam (2011)
2012	23%	-	Peng <i>et al.</i> (2003)	35%	<1	Nuryanah and Islam (2011)

Actually, the issue of governance is critical in Oman. Therefore, the Omani prime minister has emphasised on the importance of transparency, integrity, accountability and openness of organisational operations in both public and private sectors. Through the above values of underpinning governance practices, Omani public and private sectors can be improved, in terms of effective and efficient performance in their day-to-day operations, thus developing a superior nation and gaining the public's trust (Al-Sasini, 2011).

The HE Chairman of the Capital Market Authority addressed the situation (in Oman in 2010). He stated that the current financial crisis highlighted the significance of corporate

governance and the public shareholding companies control practices and behaviours on different levels of functions. Governance creates a sense of responsibility and belonging among the companies' employees and encourages ethical rules to protect the shareholders and other relevant parties' rights. Terms that blur their work strategy and their outcome affect their work and the company as a whole along with its affiliations and resulted in the vulnerability and bankruptcy of banks and financial companies and investments in the region (Bataineh, 2010).

Ultimately, the issue of corporate governance is now the core subject for business leaders and regulators worldwide, particularly following the global financial crisis. The crisis has led to many instances of collapse of corporate governance and thus, international regulators are expanding efforts to influence suitable regulatory controls. This clarifies the invaluable role of effective corporate governance in the whole society (Ibrahim, Rehman & Raoof, 2010).

As such, a significant emphasis is upon the practice of corporate governance, which various writers have cited as the answer to the issues in the countries' market environment. The majority of the studies from different fields, including accounting, economics, administrative, legal and others have been carried out on the subjects of corporate governance, its benefits and positive outcomes (La Porta, Lopez de-Silanes, Shleifer & Vishny, 2000).

Empirically, the literature regarding the relationship between corporate governance and firm performance has been extensive in the developed countries, but there are limited studies in developing countries. However, the findings regarding this relation is found to be inconclusive and the literature is still insufficient in the emerging markets such as Oman. One literature stream finds that corporate governance is positively associated with the firm performance (e.g. Ali & Nasir, 2014; Al-Najjar, 2013; Al-Najjar, 2014; Azam, Usmani & Abassi, 2011; Bozcuk, 2011; Chahine & Safieddine, 2011; Ghahroudi, 2011; Danoshana & Ravivathani, 2014; Heenetigala & Armstrong, 2011; Ibrahim & AbdulSamad, 2011; Kang & Kim, 2011; Khan, Nemati & Iftikhar, 2011; Khatab, Masood, Zaman, Saleem & Saeed, 2011; Liang, Xu, & Jiraporn, 2013; Mahadeo, Soobaroyen & Hanuman, 2012; Mehraban & Dadgar, 2013; Müller, 2014; Obiyo & Lenee, 2011; Pissaris, Jeffus & Gleason, 2010; Shahab-u-Din & Javid, 2011; Swamy, 2011; Uwuigbe & Olusanmi, 2012).

Contrarily, other studies show a negative relationship between corporate governance and firm performance (e.g. Ali & Nasir, 2014; Evans, Nagarajan & Schloetzer, 2010; Chechet, Jnr & Akanet, 2013; Danoshana & Ravivathani, 2014; Jermias & Gani, 2014; Garcí'a-Meca & Sa'nchez-Ballesta, 2011; Herly & Sisnuhadi, 2011; Liang, Xu, & Jiraporn, 2013; Muravyev, Talavera, Bilyk & Grechaniuk, 2010; Sahu & Manna, 2013; Rachdi & Ameer, 2011; Sheikh, Wang & Khan, 2013; Switzer & Tangb, 2009; Valenti, Luce & Mayfield 2011; Vo & Nguyen, 2014; Wang & Oliver, 2009). Far from previous findings, there are some researchers who have found that there is no relationship between

corporate governance and firm performance (e.g Al-Najjar, 2013; Bhagat, Bolton & Subramanian, 2011; Chowdhury, 2010; Gibson, 2003; Herri, 2011; Kaur, 2014; Kiel & Nicholson, 2006; Latief, Raza & Gillani, 2014; Latief, Raza & Gillani, 2014; Sahu & Manna, 2013; Shao, 2010; Vo & Nguyen, 2014; Wei, 2007). Thereupon, this study would re-examine the relationship between corporate governance and firm performance. Moreover, regarding extensive dissociation, this study aims to fill the gap in the literature review by conducting the relationship between corporate governance and firm performance particularly in Oman.

1.3 Research Questions

This study attempts to shed a light on the structural association between corporate governance and firm performance in Omani listed companies for effective decision making. The study particularly addresses the following research questions:

1. What is the relationship between the board of director's characteristics (size, independence, meeting, the board change, role of secretary on the board, the legal counsel and foreign member on the board) and the firm performance of Omani listed companies?
2. What is the relationship between the audit committee characteristics (size, independence and meeting) and firm performance of Omani listed companies?

3. What is the relationship between the executive committee existence and firm performance of Omani listed companies?

1.4 Research Objectives

In order to answer the questions of the study as posed in the preceding section; this study aims to achieve the following objectives:

1. To investigate the relationship between board of directors' characteristics (size, independence, meeting, board change, the role of secretary on the board, the legal counsel and foreign member on the board) and firm performance of Omani listed companies.
2. To examine the relationship between the audit committee characteristics (size, independence and meeting) and firm performance of Omani listed companies.
3. To investigate the relationship between the executive committee's existence and firm performance of Omani listed companies.

1.5 Significance of the Study

This study potentially contributed to the literature, as it is a comprehensive representation of the relationship between corporate governance and performance. In general, this study has prospective significance as follows:

1.5.1 Theoretical Significance

This section provided potential theoretical significance of the present study. Firstly, this study clarifies the understanding concerning the best practices of corporate governance structure in Omani listed companies. It also determines the corporate governance variables and their influence upon the organisations' performance and productivity. More specifically, the study proposes benefits to financial practitioners (investors and creditors) and academics.

Over and above, the findings of empirical studies that have been carried out in the US, UK, Chile, Hong Kong and other countries regarding firms' performance were found to be mixed while the studies of corporate governance mechanisms in Omani listed companies are inadequate. Thus, by conducting this study, invaluable findings will be revealed, which will help to enrich the level of corporate governance agenda, especially in emerging countries like Oman. Particularly, this study uses a sample of Omani companies. Hence, the findings may also provide useful information for comparative studies of the listed company's performance in other countries. Up till now, there is a lack of studies concerning firm performance in Oman. The findings of this study may explain the level of the company's performance and the corporate governance in Oman. Moreover, to the knowledge of the researcher, this study is only one of the few studies in the gulf countries in general (Al-Hussain & Johnson, 2009; Aljifri & Moustafa, 2007; Al-Matari *et al.*, 2012a; Al-Matari *et al.*, 2012b; Al-Matari *et al.*, 2012; Al-Najjar, 2013; Ghabayen, 2012; Najjar, 2012) and the unique study in Oman in particular that elaborates

the corporate governance and its impact on corporate performance in Oman (Al-Matari *et al.*, 2012a).

Prior studies have also just focussed on studying the relationship between the board of directors with audit committees and firm's performance (Abdurrouf, 2011; Al Manaseer *et al.*, 2012; Ii *et al.*, 2012; Kang & Kim, 2011; Nanka-Bruce, 2011; Obiyo & Lenee; 2011; Yasser, Entebang & Mansor, 2011). However, this study adds new variables such as, the executive committee that may enhance firm's performance.

Besides, previous studies have focused only on the effect of board of directors' characteristics such as the size of the board, the board independence and the board meeting on firm performance (e.g. Hsu & Petchsakulwong, 2010; Ibrahim & AbdulSamad, 2011; Jackling & Johl, 2009; Kang & Kim, 2011; Khan & Javid, 2011; Kota & Tomar, 2010; Lin, 2011; Nanka-Bruce, 2011; Nuryanah & Islam, 2011; Rachdi & Ameer, 2011; Reddy *et al.*, 2010; Saibaba & Ansari, 2011; Shah, Javed & Abbas, 2009; Siala, Adjaoud & Mamoghli, 2009; Yasser, Entebang & Mansor, 2011). Thus, the present study also adds new variables to the board of the directors' characteristics such as, the board change, the role of secretary on the board and the legal counsel. In addition, regarding the importance of the foreign member of the board, this study adds this variable to the board of director's characteristics because it may enhance firm's performance.

Furthermore, in terms of theory contribution, this study highlights the agency theory, resource dependence theory and corporate governance perspective in relation to firm's

performance. Studies such as Bektas and Kaymak (2009), Douma, George and Kabir (2006), Kyereboah-Coleman (2007), Lawal (2012), Lin (2011) and Major and Marques (2009) only discussed the importance of resource dependence theory in relation to the firm's performance. Furthermore, this study demonstrates that the resource dependence theory complements the other theory, namely the agency theory. Regarding this relation, Al-Matari *et al.* (2012a) suggested to examine the relationship between corporate governance and firm performance through these theories.

This study also focuses on the testing of non-financial sectors as many of the prior studies did (Abdurrouf, 2011; Al-Matari *et al.*, 2012a; Al-Matari *et al.*, 2012; Azam, Usmani & Abassi, 2011; Bøhren and Strøm, 2010; García-Sánchez, 2010; Ghabayen, 2012; Imam & Malik, 2007; Khan & Javid, 2011; Khanchel, 2007; Mandacı & Gumus, 2010; Millet-Reyes & Zhao, 2010; Prabowo & Simpson, 2011; Shahab-u-Din & Javid, 2011; Shan & McIver, 2011; Siala, Adjaoud & Mamoghli, 2009; Wahla, Shah & Hussain, 2012). Moreover, the widely previous studies used a cross sectional or time series, this study however, is significant to utilise a panel data regarding many benefits that are mentioned in the methodology chapter.

More importantly, Oman is the first GCC country to implement Code of Corporate Governance (Hawkamah on CG). This justifies the selection of such country in the investigation of the relationship between corporate governance and firm's performance. Moreover, the control variables (firm size, debt, industry and years) and their moderating

effect on the relationship between internal corporate governance and firm performance are supposed to be examined.

The present study also contributes to the few studies that are related to firm performance and corporate governance in Omani setting. Thus, by conducting this study, it is hoped that findings can enhance the body of knowledge concerning the corporate governance area and Omani firm performance. This study may also turn into useful information available to regulators, investors and the public at large on the situation of corporate governance and firm performance in Oman. Furthermore, this study is an attempt to fill the gap in prior literature by highlighting the set of governance standards for the firms with specific scores of corporate governance and to tackle issues specific to the companies.

1.5.2 Practical Significance

This section discusses potential implications of this study for financial practitioners. The present study will hopefully improve the practitioners' understanding of the corporate governance mechanisms that influences firm's performance. This study will be an addition to academics' knowledge by establishing evidence relating to corporate governance mechanisms and their influence upon the performance of the firm. The necessity to enhance firm's performance has instigated the significance of this study by determining factors that influence firm performance.

Moreover, the expected findings of the study would be useful for the companies, the policy makers and regulators in Oman (for example, CMA, Omani Organisation of Certified Public Accountants) in providing information on the effectiveness of the board of directors, the audit committees and the executive committees and their effect on the firm's performance in order to excel corporate governance practices in Oman.

1.5.3 Policy Making Significance

As the main objective of this study is to provide a comprehensive model to identify the determinants of firm performance, this study has a significant value for the policy market. Policy markets in Oman have to have this as a guideline in understating the determinants of the firm's performance. The results of this study are expected to provide the Omani policy market the bright insights into regulations that should be set up to boost the overall economy of the country.

1.6 Definition of Terms

1.6.1 Firm Performance

Return on Assets ratio (ROA): Earnings before tax divided by total assets of the company (Ali & Nasir, 2014; Al-Matari et al., 2012; Al-Matari et al., 2012a; Kaur, 2014; Müller, 2014; Saibaba & Ansari, 2013).

Tobin-Q Ratio TOBINSQ: The market value of equity plus the book value of the debt divided by the book value of the total assets (Al-Matari et al., 2012a; Al-Matari et al., 2012b; Jermias & Gani, 2014; Kamardin, 2009; Vo & Nguyen, 2014).

1.6.2 Corporate Governance Mechanisms

1.6.2.1 Board of Director's Characteristics

1.6.2.1.1 Board Size

It has been defined by Al Manaseer et al. (2012), Danoshana and Ravivathani (2014), Liang, Xu, and Jiraporn (2013), Nanka-Bruce (2011), O'Connell and Cramer (2010) and Rachdi and Ameer (2011) to be the number of directors on the board.

1.6.2.1.2 Board Independence

It is defined as the number of independent non-executive members positioned in the board relative to the total number of members (Al-Najjar, 2014; Jermias & Gani, 2014; Liang, Xu, & Jiraporn, 2013; Müller, 2014).

1.6.2.1.3 Board Meeting

The board meeting represents the number of meetings the board has during a year (Danoshana & Ravivathani, 2014; Liang, Xu, & Jiraporn, 2013; Sahu & Manna, 2013).

1.6.2.1.4 Board Change

The board change is defined as the appointment of a new member in the board during a year and is measured by using a dummy variable. If the board has a new appointment during a year, the values assigned will be (1), otherwise 0).

1.6.2.1.5 The Role of the Secretary of the Board

The role of secretary of the board is crucial and is measured by using a dummy variable. If the board has a secretary, the values assigned will be 1, otherwise 0.

1.6.2.1.6 Legal Counsel

The role of legal counsel is crucial in the board and is measured by using a dummy variable. If the firm has a legal counsel, the values assigned will be 1, otherwise 0.

1.6.2.1.7 Foreign Member on the Board

It can be measured by the number of non-executive foreign directors divided by the total number of board members (Miletkov et al., 2011; Ruigrok et al., 2007).

1.6.2.2 Audit Committee Characteristics

1.6.2.2.1 Audit Committee Size

It is measured by the number of members serving on the audit committee of the firm (Al-Matari et al., 2012; Bauer, Eichholtz & Kok, 2009; Danoshana & Ravivathani, 2014;

Ghabayen, 2012; Hsu & Petchsakulwong 2010; Nuryanah & Islam, 2011; Obiyo & Lenee, 2011).

1.6.2.2.2 Audit Committee Independence

The audit committee independence is measured through the ratio of non-executive members of the committee (Abdullah, Shah & Hassan, 2008; Al-Matari et al., 2012a; Al-Matari et al., 2012b; Chechet, Jnr & Akanet, 2013; Ghabayen, 2012; Kang & Kim, 2011).

1.6.2.2.3 The Audit Committee Meeting

It can be measured by the frequency of number of meetings during a year for the audit committee (Al-Matari et al., 2012b; Chechet, Jnr & Akanet, 2013; Hsu & Petchsakulwong, 2010; Khanchel, 2007; Kyereboah-Coleman, 2007; Rahmat, Iskandar & Saleh, 2009; Saibaba & Ansari, 2013).

1.6.2.3 The Executive Committee Existence

The executive committee's existence is measured by using a dummy variable. For instance, if the company has a committee, the values assigned will be (1), otherwise (0).

1.6.3 Control Variables

1.6.3.1 Firm Size

It can be measured by the natural log of total assets (Haniff & Huduib, 2006; Peng, Li, Xie & Su, 2010).

1.6.3.2 Leverage

It can be measured by the ratio of total liabilities to total assets (Karaca and Ekşi, 2012; Khatab et al., 2011; Najid & Abdul Rahman, 2011; Wahla et al., 2012).

1.6.3.3 Industry

It can be measured by a dummy variable; 1 if the firm is an industry and 0 for others (Chen, 2006; Tarn & Tan, 2007).

1.6.3.4 Time Period

It can be measured by a dummy variable, take value of one for the specific year and zero otherwise (Gupta & Sharma, 2014).

1.7 Scope of the Study

By and large, this study targets the companies listed on the Muscat Securities Market (MSM) and their mechanisms in generating domestic-led investment to stimulate economic development. The study is conducted only among listed companies that are

operating in the non-financial sector in the main board of Muscat Exchange Stock 2008, 2009, 2010, 2011 and 2012. The Muscat Securities Market (MSM) contains 123 companies which are distributed among financial sector, comprising of 32 firms, and non-financial sectors, comprising of 87 companies (49 industry sectors and 38 service sector). Regarding availability of data, the data used comprised of 78 firms for five years, namely 2008, 2009, 2010, 2011 and 2012. Therefore, this study aims to cover the non-financial sector. Subsequently, this data is comprised of 390 companies during five years (2008 to 2012) as provided in Table 1.2.

Table 1.2
The Scope Of Study

Year	No. of the firms	Availability
2008	87	78
2009	87	78
2010	87	78
2011	87	78
2012	87	78
Total	435	390

Finally, the study considers the following determinants of the corporate governance, board of director's characteristics (size, independence and meeting, board change, the role of secretary on the board, legal counsel and foreign member on the board), the executive committee and audit committee's characteristics (size, independence and meeting). In terms of firm performance, this study focuses on common measurement such as ROA and Tobin-Q.

1.8 Organisation of the Study

Chapter one comprises an introduction to the study, which includes elaboration of the research background, problem statement, research questions, research objectives, significance of study, study scope and the organisation of the study.

The next chapter (Chapter Two) provides insight into the background of Oman, economic brief in gulf cooperation council (GCC) states, corporate governance in emerging markets, performances in gulf cooperation council market, corporate governance in Oman and summary of the Chapter Two.

Chapter Three tackles the literature review. The subjects discussed in this chapter are firm performance (including firm performance definition and measurement), the importance of performance, corporate governance (together with corporate governance definitions and corporate governance importance), the relationship between corporate governance i.e. board of directors' characteristics (board size, board independence, board meeting, board change, the role of the secretary on the board, the legal counsel foreign member on the board), audit committee' characteristics (size, independent and meeting), the executive committee and firm performance. Finally, this chapter provides the underpinning theory for this study. This chapter end with the summary of the chapter. The Chapter Four debates the research framework and hypotheses development, including theoretical framework, hypotheses development, namely, firm performance, the board the of directors characteristics and firm performance, audit committee

characteristics and firm performance, the executive committee and firm performance, control variables and summary of the chapter.

Chapter Five provides research methodology that covers research design, panel data, data collection procedure, unit of analysis, model specification and multivariate regression, measurement of the variables, the proposed data analysis technique. Lastly, the chapter summary is provided.

Chapter Six comprises responses, companies profile, descriptive statistics, correlation analysis, testing for panel data, results of LM test, results of f test, the results of Hausman test, GLS estimation, model estimation, evaluation of the models, hypothesis testing, summary of hypothesis testing: corporate governance and firm performance, models equation. Lastly, in the end there is chapter's summary.

Chapter Seven discusses summary of the study, discussion of the first model (results based on accounting measure), discussion of second model (results based on marketing measure), implications of the study, namely implications to theory, implications to practice and implications to policy making, limitations of the study and suggestions for future research and conclusion of the study.

CHAPTER TWO

BACKGROUND OF OMAN

2.1 Introduction

This chapter highlights information regarding Oman i.e. background of Oman, economic view, economy growth, foreign direct investment (FDI), inflation, financial situation, currency and external account. It also provides a summary of the economic situation in the gulf cooperation council (GCC) states, corporate governance in emerging markets, performances in GCC market and corporate governance in Oman. A summary of the chapter is provided in the final section.

2.2 Background of Oman

Oman, a country located in the southwest Asia to the Southeast of the Arabian Peninsula, is bordered by the United Arab Emirates (UAE) to the northwest, the Kingdom of Saudi Arabia to the west, Yemen to the southwest, the Arabian Sea coast to the Southeast and the Sea of Oman to the northeast. It borders with UAE on the Musandam region only and continues to form the coastal areas and the Strait of Hormuz and the Gulf of Oman Musandam borders (Cabinet, 2010). From an earlier period, Oman has been a moderate regional power and was extended through the Strait of Hormuz all the way to Iran and Pakistan and the modern day Zanzibar in the Southeast African coast (Kharusi, 2012). Over time, with the decline in strength, the Sultanate became under the influence of the

United Kingdom (UK), although Oman is no longer officially under the British Empire or under its protection (Cable, 2011). The Omani royal family claims that the Sultanate of Oman was under the rule of the Al Said dynasty since 1744. However, there is no concrete evidence. Oman maintains a long-term independent foreign policy despite the military relations and political relations with the UK and United State (US) (Kharusi, 2012). The system being in practice in Oman is the monarchy where absolute power is exercised by the Sultan of Oman, but its parliament has some legislative powers and controls (Bonn, 2012). In November 2010, the United Nations Development Program (UNDP) listed Oman among 135 countries all over the world, as the most improved nation during the past 40 previous years (UNDP, 2011). On the basis of international indicators, the Sultanate of Oman is considered among the developing countries that are stable.

Oman is among the Middle Eastern countries blessed with considerable natural resources, particularly, oil and natural gas. It has a significant trade surplus along with low inflation. The Omani government is also an advocate of liberalization of markets, which drives the process of privatisation in the country. Privatisation of utilities as well as economic diversification is under way in the hopes of attracting foreign investment. More importantly, Oman joined the World Trade Organisation (WTO) in November 2000 (Al-Rimawi, 2001).

With regards to the oil production, Oman produces approximately 700,000 barrels of oil on daily basis, representing around 90% of the country's exports. With promising

economic conditions, owing to high oil prices, Oman is currently struggling to build its infrastructure.

Oman's distinctiveness lies in the fact that, being an oil-producing nation in the Middle East, it is not an OPEC member. The country is exerting much effort in diversification of resources and aims to contribute more from the non-oil sector in the coming years. At present, oil's contribution constitutes around 33.5% of the GDP, which will decrease to 9% by 2020. Therefore, the government is trying to contribute more in terms of natural gas and the manufacturing sector to the GDP (Al-Rimawi, 2001).

2.2.1 Economic View

The economy of Oman is characterised as a middle-income economy with the substantial presence of oil and gas resources, and significant budget and trade surpluses. Oil constitutes 64% of total export earnings, 45% of government revenues and 50% of GDP. It is therefore not surprising that the petroleum products sector is among the most significant sectors in the country's economy. Furthermore, Oman owns 5.50 billion barrels of crude oil reserves accounting for 1.2% of the total crude oil reserves in the GCC region and around 0.4% of the world's oil reserves.

Presently, Oman's oil production level is measured at 0.806 million barrels per day, but is expected to be depleted in the next 19 years. The best period of economic development was reported to be between 2003 and 2008, in light of economic performance backed by high oil prices, which in turn, assisted in developing budget surpluses, trade surpluses and

foreign reserves (Bonn, 2012). Oman has a particular sector characterised by force, diversity and encompasses activities such as industry, agriculture, retail and tourism, and industries such as copper mining, smelting, oil refinement and cement factories. Oman also seeks to attract foreign investors to its industry, information technology, tourism, and higher education. The country's industrial development plan includes gas resources, manufacturing of iron, petrochemicals and international ports.

The main challenges faced by Oman currently have currently been high liquidity and high inflation till late year 2008. Moreover, the financial crisis led to global economic decline and the decline in budget surpluses in 2009. As a consequence, Oman had to slow down its investment and development projects. However, despite the adverse global situation, Oman succeeded in using technology gains to increase oil production and worked towards economic diversification. Oman is also attempting to diversify its industries and private sector to gear up for the expected depletion of the oil sector's contribution to the GDP in 2020 (Palazhi, 2012).

2.2.1.1 Overview of Macroeconomic

2.2.1.1.1 Economy Growth

The continuous increase in oil prices from year 2003 contributed to the significant growth in the economy of Oman, which doubled in size from 2003 to 2008. Nominal GDP growth rate showed an increase of 44% to achieve USD 60 billion in 2008 compared to USD 41.6 billion the previous year. However, due to the financial crisis and decline in

the global economy and world oil market in 2009, the nominal GDP of Oman decreased by 10.9% to USD 53.4 billion. It was expected to increase by 16.6% by 2010 and 8.9% by 2011. The economy showed a 3.4% growth in 2009 compared to 6.2% in the previous year and was expected to grow further by 4.7% in 2010 and 2011 with the recovery from the global crisis and the increasing global demand for oil (Salman, 2011).

2.2.1.1.2 Foreign Direct Investment (FDI)

In Oman, the foreign direct investment inflows were reported at 1.10% as of 2011 based on the World Bank report, 2012. FDI or foreign direct investment refers to the net inflows of investment to obtain a lasting management interest (10% or over the voting stock) in a business operating in an economy different from that of the investor. It is the total of equity capital, earnings reinvestment, other long-term capital and short-term capital as revealed in the balance of payments. The series depicts net inflows (new investment inflows less disinvestment) in the economy from foreign investors over GDP.

Oman is characterised by a strong macroeconomic situation where GDP growth in 2011 was 5.5%, expected to be 5% in 2012 because of the average oil price at USD 102/barrel. In addition, credit growth doubled in 2011, and the financial system's well capitalisation was maintained with minimal non-performing loans at 2.6% below the GCC average. Also, Oman boasts of a stable A1 credit rating with very low external debt at 3 to 4% to GDP, which is considered as among the lowest in the world. Based on the report of Public Authority for Investment Promotion and Export Development (PAIPED), new

FDI in Oman increased to RO5 billion, approximately USD16 billion in 2010, from RO980 billion (USD 2.5 billion) in 2003.

Although systematic information regarding FDI is limited, according to the Public Authority for Investment Promotion and Export Development (PAIPED), FDI increased to USD16 billion in 2010 which is approximately 20% of GDP with UK as the top source of investment (33%), followed by the US (20%). As reported by the Capital Market Authority statistics in December 2009, foreign participation with the inclusion of GCC nationals was recorded at 23% in light of shares in the Muscat Securities Market (MSM). Moreover, foreign capital constituted 24% of the financial shares, 21% in manufacturing and 23% in insurance and services. FDI exhibited a significant increase over a decade of a mere RO929 billion (USD 2.4 billion) in the year 2003.

2.2.1.1.3 Inflation

The country's liquidity inflation has remained low, ranging between -1% and 1.9% from the year 2001 to 2005, but showed an increase of 12.6% in 2008 compared to the previous year, which was recorded at 5.9%. This is attributed to imports of goods priced in Euro, Japanese Yen and the British Pound along with the dollar devaluation against major currencies in the world. The monetary policy of the country focuses on controlling inflation, which can be described as mild owing to the country's level of economic openness. Government controls the prices of goods through support and it refuses to employ currency instrument to cover its budget deficit. Hence, there is little inflation and

inflation has in fact decreased while the consumer price index rose to 3.5% in 2009 due to Oman's monetary and fiscal policies. The Omani Rial (OMR) is tied up with the USD because the US is the most important source of import. The Omani Rial peg protects US prices of some imported inflationary pressures from America. It was expected that the annual inflation rate would rise in consumer prices to 3.9% in 2010 and to 2.9% in 2011 (GulfBase, 2013).

2.2.1.1.4 Financial Situation

In Oman, public finance is highly reliant on oil revenues, as it constitutes 67% of public income. Additionally, the government appropriated budget has a major role in the processes of resettlement, diversification and privatisation. The Omani government discerned an on-going deficit in the budget from 1992 to 2001. Following this period, the Omani economy began noticing surplus budget of 9.6% of GDP in 2008 (compared to 13.7% in the previous year) owing to higher oil revenues and appropriate policies by the sound financial background professionals. However, by the following year (2009) Oman failed to achieve a budget surplus because of the financial crisis and the global economic decline in the oil market. But, owing to the global economic retrieval, financial surpluses were expected to reach a surplus of 4% of the GDP in 2010 and 2011 (Cable, 2011).

2.2.1.1.5 Currency

The official currency of Oman is the OMR and it has been linked to the USD since 1973. In January 1986, after a devaluation of 10.2%, the currency exchange became fixed, with

one OMR equal to USD2.60. This assisted in lowering inflation and the government policy maintains this exchange with a total reserve of USD11.5 billion, as reported in 2008, compared to USD9.5 billion in 2007. By the end of 2009, the reserve was reported to be USD11 billion and was expected to reach USD11.1 by the end of 2010 and USD11.5 the year after (Palazhi, 2012).

2.2.1.1.6 External Account

High prices of oil culminated in huge trade surpluses in the current account of the years 2005 to 2008, where it has been reported to reach USD5.47 billion in 2008 (approximately 9.1% of GDP) in comparison to USD2.59 billion (approximately 6.2% of GDP) in the previous year. By 2009, a slight surplus of USD0.14 billion (approximately 0.3% of GDP) was achieved by the economy. This figure was expected to reach USD 1.48 billion by 2010, and USD 2.14 billion by 2011 considering the recovery of the global oil market. The account balances are also affected by the considerable transfers of foreign workers and the profit remittances of foreign companies like the Oman Petroleum Development along with the foreign private sector companies (Palazhi, 2012).

2.3 Economic Brief in Gulf Cooperation Council (GCC) States

The Gulf Cooperation Council (GCC) region depends mainly on oil, as it possesses the world's largest oil reserves with an estimated 486.8 billion barrels, which is equal to 35.7% of the total crude oil reserves in the world and 70% of the total OPEC world reserves. This positions the region as one of the largest producers and exporters of oil. It

plays a leading role in the world and in OPEC. Until late 2008, the GCC exhibited six massive spurts in the economy. The economy was double in size at USD1.1 trillion from the period 2002 to 2008 with a reserve ratio of 52% of the total OPEC oil reserves and produced 49% of the total OPEC oil production. The oil and gas exports were around 73% of total export earnings.

For the GCC countries, the oil and gas sector make up around 63% of government revenues and 41% of GDP. In addition, the decreased average annual oil price for the OPEC basket in 2009 increased to 35.4% a barrel compared to 2008, where the annual average was USD94.45, owing to the financial crisis, the global economy and the decreasing global energy demand. On July 11, 2008 in New York, the price of crude oil reached its highest price i.e. 147.27USD a barrel. This was followed by a fall in price, by an average annual price of crude oil for the OPEC basket in the initial four months of 2010 at 77.20USD/barrel compared to 2009 at the same period (44.79USD) and at 78.47USD compared to the same period in 2009 (45.95USD). In 2010, it also reached 80.18USD (US crude oil) compared 2009 (44.71USD). The region continues to follow plans for the implementation of economic reforms and is currently focussing on attracting local private sector, investments from the region and from other countries, generating gas and power, telecommunications and real estate sector. Though, the world oil market shows evidence of decreasing owing to the financial crisis and global economic slowdown, the market shows promising investment and development projects which are intended to aid in the region's fast economic recovery.

2.4 Corporate Governance in Emerging Markets

Emerging economies should consider employing corporate governance (GC) mechanisms in order to develop investors' confidence to attract both, foreign and local investment and to expand trade (Abhayawansa & Johnson 2007). Developing countries are indirectly urged by international donor agencies, including the International Monetary Fund (IMF), the World Bank and Organization of Economic Cooperation and Development (OECD) to enhance their corporate governance mechanisms and regulatory infrastructure (Athukorala & Reid, 2003). Moreover, the adoption of corporate governance was also driven by the notion that the economic crisis experienced by the South East Asian stock markets in 1997 to 1998 was attributed partially to ineffective corporate governance (Mobius, 2002). Hence, governance reforms were adopted in the emerging markets to restore investor confidence through the provision of a secure institutional platform upon which the investment market could be built (Monks & Minow 2004). Kashif (2008) highlighted the important role the corporate governance plays in enhancing the firm's performance in both developed and developing nations. He reached such a conclusion upon conducting a comparison between the two categories of nations. He also revealed a slight difference between the relation of corporate governance and the value of firms among their financial markets, which stems from the differences in their CG structures as each country exhibits distinct social, economics, laws and order situations. CG is favourable for the effective use of assets in improving the firm value. Moreover, the large

board size drives the firms in developing financial markets while small board size and less debt drive the firms in developed ones (Ibrahim, Rehman & Raof, 2010).

2.5 Performances in Gulf Cooperation Council Market

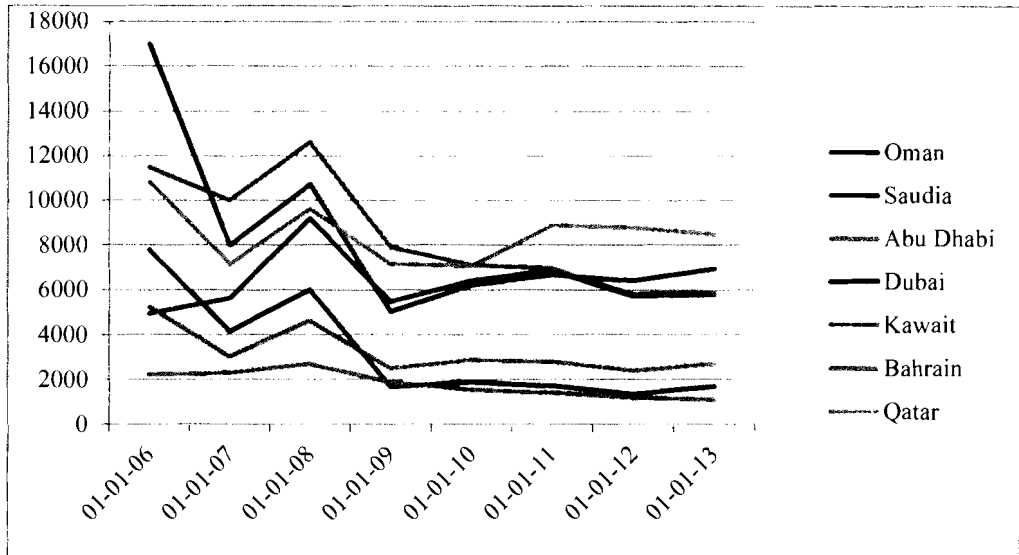


Figure 2.1
The Performances in GCC Market
 Source: GulfBase (2013)

A thorough review of the Gulf market's performance in the current period reveals that the overall performance experienced fluctuation and significantly declined at the end of 2009 on the basis of the current available data as depicted in Figure 2.1. Along with the impact of the global fiscal crisis, this declining and fluctuating trend can be ascribed to the lack of capital, needed for business expansion and running, owing to the decline of FDI inflows stemming from the investors' lack of confidence in the Gulf companies' corporate governance mechanisms. Stated differently, the ineffective corporate governance mechanisms in the Gulf business environment prevented the improvement of

companies' performance. This situation requires more studies to be conducted in the Gulf region to examine the level to which corporate governance could impact the firms' performance in different business sectors.

According to the above Figure 2.1, the Omani companies' performance has been outstanding during the economic crisis and the volatile situation. The evident decline in investment in the country is attributed to the lack of confidence of investors, which led to the landslides in Gulf companies. Omani companies however, showed the best performance prior to 2008, but following that year, their performance decreased due to the lack of confidence and the weak state of control over the adoption and application of corporate governance law. Intrinsically, the present study investigates the relationship between corporate governance and performance of the firm.

2.6 Corporate Governance in Oman

On scrutinising the stages of passing laws and regulations within Oman, it is evident that Oman is working to realise an investment environment that is conducive to the national economy's recovery. Oman initiated its enacting of laws in the following order; Commercial Companies Law 1974, the Capital Market Law 1988, Law of Public Bodies and Institutions issued by the Royal Decree in 1990, the Charter of Organisation and Management of Public Companies 1991, Act of Foreign Capital Investment (FCI) by Royal Decree in 1994, Arbitration Act in Civil and Commercial Disputes by Royal

Decree in 1997, the Law of Muscat Securities Market (MSM) Decree 1998 and finally the Charter of the Organisation and Management of Public Companies 2003.

Back in the 1970s, sole proprietorships and partnerships were the predominant types of commercial enterprise in the Omani business environment. Even with incorporated enterprises, the company owners did not intend to sell the shares to the public. After fourteen years of the enactment, in 1988, the MSM was created and it initiated operations with a total of eleven listed companies and securities worth OMR28,452,000 (USD73,975,200).

In 2001, several additional substantive changes occurred; the CMA issued a notice mandating companies to either disclose information concerning the estimates of audited, unaudited results and other relevant materials affecting the results, or guarantee that the information will be kept secret so that no inside trades can be carried out and there will be no exchange of information with others (CMA, 2001). The mandate included an attachment of the revised rules explaining disclosure standards and requirements for unaudited accounts. In April of the same year, the MCI laid down the executive regulations of the CMA to provide guidance on the securities issuance and other elements of the securities market. This was followed in August by the transference of reference from the Modern Cold Industrialisation (MCI) to CMA concerning the public joint stock companies' supervision and the CMA distributed circulars regarding its policies for disclosure, qualifications and responsibilities of directors and the general meeting guidelines. In September, the CMA adopted new conditions for MSM listings.

After the establishment of MSM, the Omani government urged local companies to extend and issue securities to the public. The situation then, as it is now, was such that several public companies were family owned with public float or held small minimum investor float. The Omani government owned some companies and the Commercial Companies Law (CCL) issued guarantees of ownership rights as the owners were reluctant to take their companies public and losing control. Therefore, a company could go public and be included in the MSM list while the owners maintained 60% of their shares (Dry, 2003).

Majority shareholders (holding 10% shares or over) were represented by the board of directors and the articles of association could be drafted so that shareholders may elect a minority of directors (Ministry of Commerce Report, 2000). If any question concerning the requirement for control by specific shareholders arises, the company is allowed to issue a type of share with superior voting rights and create various classes of shares providing the shareholders of every type, the right to vote for any of the members of the board (Dry, 2003). Moreover, joint stock companies could be established and go public and be on the list of MSM. Therefore, on the basis of the above information, the corporate governance assisted in arranging the relationship between management and owners and to do two distinct jobs to improve companies' performance (family owned or public).

The Oman capital market is experiencing significant changes in the current times. The Capital Market Law was amended to allow additional disclosure and to extend the board of directors' authority of the CMA concerning the listed companies' discipline. This was

followed in June, by the issuance of the Corporate Governance Code by the CMA that was applicable to firms whose securities were included in the MSM list. H.H. Sultan Qaboos, the King of Oman, issued the 2002 CCL Amendments in August, which addressed issues pertaining to the composition of the BOD and internal controls (CMA, 2001). Generally speaking, corporate governance (CG) codes are considered the main instrument for the restoration and maintenance of public as well as investors' confidence all over the globe and the promotion of effective management. This is because of the fact that effective corporate governance attracts investors, provides them and other stakeholders' protection and enhances the company's value.

CG codes have become the primary instruments of restoring and maintaining public and investors' confidence on a global scale and the promotion of effective management. This is because effective corporate governance works to attract investors, to protect them and other stakeholders and to improve the value of the company. In fact, the pioneering code in the GCC was issued by Oman in 2002 and by Bahrain in 2010 (Hawkamah on CG). The department's development took place in 2007 to tackle issues of governance, to establish greater awareness and follow-up the progress of practices and reinforcement of the organisations based on the latest international standards and practices. Moreover, in 1996, Oman adopted the International Accounting Standards (IASs) as the Sultanate Decree of National Accounting Standards (Hawser, 2005).

At the first glance, the stock market appears to be intensively working on developing a list of governance and identifying the main points of the manner the regulation will be

applied to the companies listed in the MSM. The corporate governance is developed based on the OECD's for upgrading the organisations in Oman. This is to create a platform to unify the foundations of effective handling and fairness to guarantee best practices, safeguard the relevant company stakeholders, increase shareholder value, and bring back confidence in the market through the upgrade of the organisation in local companies along with their financial performance and management. The charter of OECD stems from the global best practices that the local economic environment is able to adopt while guaranteeing the values of transparency, responsibility and continuous maintenance that are consistent with the best global practices (Dry, 2003).

The corporate governance is developed according to the job segregation and the protection of shareholders' rights. The regulation is created with the help of the terms of reference and functions of the council as the board of directors is considered the most important council in the company for its crucial role in achieving goals. It is considered the core of the implementation of the company's objectives. Additionally, the governance works primarily on the importance of functions separation for the achievement of the principles of integrity and transparency. For instance, some committees within the council work to control and oversee the administrations in the company and conduct an evaluation and report to the council. This is to ensure that crisis measures are taken and the firm performance is improved. Moreover, the reason behind the CG stress on the significance of full disclosure of all shareholders in terms of all matters in a permanent and honest way, making them aware of their work and implementation level. Hence,

disclosure has a key role in the process of investor attraction at the local and international level (Darwish, 2007).

In the Omani environment, the concept of CG is clear in developing an effective role and an efficient entity of the capital market. Through the current laws and regulations, it stresses on transparency in accounting procedures and financial audits and it maximises the support of government for public joint stock companies to ensure that governance helps achieve several benefits with the inclusion of economic development and highlighting fraud and corruption (Dry, 2003).

Moreover, market authority supervises and controls companies by mandating governance for listing and by urging commitment to laws and regulations applicable in the country to improve governance. Consequently, this results in minimising the issue of conflict of interest and in enhancing economic efficiency, including a set of relationships between the management of the company, their shareholders and other relevant parties. The Omani companies' commitment to the principles of the Charter is exhibited through their formation of a governing council and in their control of auditing and internal mechanisms. This achieves the governance criteria of transparency and responsibility, which results in the provision of data and information encapsulated in the company's financial statements. This depends upon by the parties dealing with the company for their decision-making processes (Omani Code of Corporate Governance, 2002).

There are many important investment incentives in the Oman Capital Market (OCM).

They include the following:

1. There are no taxes on capital returns or profits.
2. There are no restrictions on the transfer of capital or profits.
3. There are no restrictions on the operations of the exchange.
4. Portability OMR exchanges linked to a fixed exchange rate with the USD.
5. Lower taxes on the profits of companies with incentives and exemptions those are rewarding and long-lasting.
6. Foreign investors can invest in stocks or mutual funds listed on the market without any prior permission.
7. The existence of an independent supervisory body to ensure a fair and stable market, to protect investors' rights and to ensure maximum transparency and integrity.

For attracting investors to Oman, there are various investment incentives enjoyed by the Sultanate of Oman namely GulfBase (2013):

1. The application of the Sultanate of a free economic system.
2. Political and economic stability.
3. The percentage of ownership from 70% up to 100% of foreigners.
4. The absence of any restrictions on the transfer of funds and profits abroad.
5. Lack of individual income tax.

6. Soft loans with low interest rates and comfortable repayment periods
7. Attractive tax exemptions for companies for up to 10 years

Finally, more information concerning the corporate governance of Oman is provided in Appendix B.

2.7 Summary of the Chapter

The chapter presents the background of Oman, location, economic view, namely, economy growth, FDI, inflation, financial situation, currency and external account. It also provides an economic summary in the GCC states, corporate governance in emerging markets, performances in GCC market and corporate governance in Oman. The literature review of this study is discussed in the next chapter.

CHAPTER THREE

LITERATURE REVIEW

3.1 Introduction

The present chapter explains firm performance, corporate governance and the association between corporate governance dimensions, namely board of directors' characteristics (board size, board independence, board meeting, board change, secretary role, legal counsel and foreign member of the board), audit committee characteristics (size, independence and meeting), executive committee and firm performance (ROA and Tobin-Q). In addition, the present chapter discusses the underpinning theories. A summary of the chapter is provided at the end.

3.2 Firm Performance

3.2.1 The Firm Performance Definition and Measurement

Performance measurement is described as the quantification of the action's effectiveness and efficiency (Neely, Gregory & Platts, 1995). It is the transference of the complex reality of performance into a chronology of limited symbols that are communicable and reported under similar situations (Lebas, 1995). However, in contemporary management, performance management occupies a more significant position that goes beyond quantification and accounting (Koufopoulos, Zoumbos, Argyropoulou & Motwani, 2008).

Performance measurement can provide information that facilitates managers' monitoring of performance, progress update, improve motivation and communication and discern issues (Waggoner, Neely & Kennerley, 1999). It is thus important for any company to analyse its complete organisational performance. But there is a lack of consistency in the area of management as to what exactly comprises organisational performance. Correspondingly according to Cameron and Whetten, (1983) business performance is invaluable in strategic management based on three dimensions i.e. theoretical, empirical and managerial dimensions.

The countless number of ways has been brought forward to measure financial performance, whether accounting based measurement or market based measurement. The accounting based measurement includes Return on Assets (ROA), Return on Equity (ROE), Return on Sales (ROS), Return on Investment (ROI), Profit Margin (PM), Operating Cash Flow (OCF), Earnings per Share (EPS), Operation Profit (OP), Growth in Sales (GRO), Return on Capital Employed (ROCE), Expense to Assets (ETA), Cash to Assets (CTA), Sales to Assets (STS), Expenses to Sale (ETS), Labour Productivity (LP), Cost of Capital (COC), Return on Revenue (ROR), Profit per employee (PPE) and Return on Fixed Assets (ROFA). On the other hand, market based measurement includes Tobin-Q, Market Value Added (MVA), Market-to-Book Value (MTBV), Abnormal Returns; Annual stock return (RET), Dividend Yield (DY), Price-Earnings Ratio (PE), Log of Market Capitalization (LMC), Stock Repurchases (SR) and Superior to Cumulative

Abnormal Returns (CARs). Most of these proposed measures have been utilised by other studies regarding corporate governance.

Based on an extensive debate concerning research methods, some researchers have recommended to study determinants of corporate governance with Tobin's-Q such as Bozec (2005), Deeksha and Ajai (2009) and Khan, Nemati and Iftikhar (2011). Conversely, there are some authors who recommend the examination of profitability measurement with corporate governance, like Khatab *et al.* (2011).

In theory, the performance is the core of strategic management, but empirically the majority of research strategies utilises the business performance construct in their investigation of various strategic content and process issues. As from the management viewpoint, performance has an evident importance from different prescriptions recommended for performance enhancement. Therefore, this study employs both measurements of performance; accounting based measurement and market based measurements as Al-Matari *et al.* (2012) recommended the same, given the importance of profitability in the short term and value of the market in the long term. Following the above discussion and recommendation, the present study aims to measure performance through two measurements, namely ROA accounting-based for a short term and Tobin-Q market-based for the long term. This integration between accounting based and market based measurement provides a clear insight into a company in the current or future times.

In addition to the above, there are various empirical studies that have adopted both accounting based measurements like ROA and market based measurement. such as Tobin-Q. For example, Abdullah *et al.* (2008), Bauer *et al.* (2009), Bektas and Kaymak (2009), Bhagat and Bolton (2009), Bhagat *et al.* (2011), Chowdhury (2010), Dey (2008), Douma *et al.* (2006), Ehikioya (2009), Garg (2007), Harjoto and Jo (2008), Heenetigala and Armstrong (2011), Herly and Sisnuhadi (2011), Irina and Nadezhda (2009), Jackling and Johl (2009), Kapopoulos and Lazaretou (2007), Khatab *et al.* (2011), Kyereboah-Coleman (2007), Liang *et al.* (2011), Lin (2011), Lin *et al.* (2011), Mandacı and Gumus (2010), Najid and Abdul Rahman (2011), Omran, Bolbol and Fatheldinc (2008), Reddy *et al.* (2010), Sánchez-Ballesta and García-Meca (2007) and Sanda, Mikailu and Garba (2005). Based on the above evidences, the present study also measures performance by using both ROA and Tobin-Q.

In the extant literature, some of the most significant measures of the firm value include Tobin's Q, which refers to the ratio of the market value of assets to the replacement value of assets. It also determines the firm value in the financial markets. Tobin-Q is measured by the market value of equity plus the book value of the debt divided by the book value of the total assets. Conversely, from an accounting perspective, the accounting based measurement is vital for firm performance in the short term. This includes ROA, which is used to determine the differential effects of CG upon the types of firm performance. ROA is also defined as the profitability ratio calculated as net income divided by the company's total assets.

3.2.2 The Importance of Performance

Broadly speaking, the firm's success is reflected through its performance, how the firm performs over a certain time. Significant efforts have been spent in the determination of measures of performance. Through the determination of such measurements, a firm is enabled to compare its performance in various instances.

Firm performance is greatly influenced by CG. If the functions are suitably set up for the corporate governance system, it will help in attracting investment, aid in increasing company's funds, strengthen the pillars of the company and in turn, this will proceed to the automatic increase of the performance of the firm. Effective corporate governance protects the firm from possible financial suffering and results in significant development. Currently, the impact of CG upon the firm's well-being is being investigated (Ehikioya, 2009).

Additionally, the firm value refers to the amount of assets that can be taken from the firm shares by the shareholders (Abdurrouf, 2011). Moreover, the performance of a company can be seen from the financial statement presented by the company. Disclosure of financial information will provide useful information for users of financial statements. Subsequently, a company with a good performance will support the management to make a quality disclosure (Herly & Sisnuhadi, 2011).

3.3 Corporate Governance

3.3.1 Corporate Governance Definitions

CG encompasses an extensive diversity of fields ranging from economics to business, law and accounting that makes it increasingly complex. The topic of CG is crucial and vital in today's investment environment. The need for the study emerged after the occurrence of several financial crises. As a result, researchers came up with several efforts to describe the CG concept. The current study offers comprehensive identifications of the definitions of CG in a multiplicity of ways with the most broadly cited descriptions listed below:

Since the pioneering work of Berle and Means (1932), CG has been concentrating on the principal-agent issues that stems from dispersed ownership in the existing firms. CG mechanisms exist within companies to improve their performance.

A current CG definition provided by Zingales and Raja (1998) defines CG as a complex set of constraints that creates the ex-post bargaining over the quasi-rents produced by the firm. In other words, the firm is the centre of implicit and explicit contracts. Incomplete contracts owing to uncertainty, informational asymmetries and contracting costs (Grossman & Hart, 1980; Hart & Moore, 1990; Hart, 1995), conflicts of interests arising from insiders and outsiders because of the separation between ownership and control, all calls for the role of CG (Jensen & Meckling, 1976).

Moreover, Cadbury (1992) describes CG as the mechanism utilised to provide discipline to the organisations and he added that it primarily handles the value creation of shareholders through the effective use of the assets of the firm. Similarly, Wolfensohn, the president of the World Bank, refers to CG as the promotion of corporate fairness, transparency and accountability (Financial Times, 1999).

In a related study; Blair (1995) refers to CG, as the complete set of legal, cultural, and institutional arrangements determining the steps which public traded corporations take, who controls them and how they are controlled, and how the risks and returns of the steps taken are allocated. Morin and Jarrell (2001) also, described CG as a framework controlling and safeguarding the relevant players' interests in the market. These players include managers, employees, customers, shareholders, executive management, suppliers and the board of directors.

In the same context, Mathiesen (2002) claimed that CG is the mechanism used to safeguard the interest of the shareholders through the provision of management incentives. CG is primarily the set of processes, customs, policies, laws and institutions impacting the direction, administration and control of a corporation (Boubakri, 2011).

Moreover, CG is defined by Denis and McConnell (2003) as a set of mechanisms in institutions and markets that impacts the self-interest of the firm's controllers – those who make decisions concerning the firm operations that increases firm value of the owners. CG is also concerned with determining a solution to the issue surrounding the principal -

agent relationship. The principal is the provider of finance and hence, he looks for ways to make sure that management activities are geared to maximise returns for them (Ehikioya, 2009).

This is consistent with Santosh (2005) who stated that CG is a framework controlled and directed by the company. In other words, CG encompasses effectiveness and efficiencies of operations, reliability of financial reporting, adherence to laws and regulations and protection of assets. It reflects the carrying out of business based on the owner's inclination, which is basically to maximise profits without compromising the societal rules, laws and local customers. Based on the OECD, CG is a method that managers and monitors companies (OECD, 2004).

In light of the above statement, the present study attempts to shed a light on the OECD principles significant to corporate performance – principles that assist in initiating the collection of national codes of CG. They concentrate on publicly traded companies, although issues concerning companies with a large number of shareholders are also addressed whether they are public or listed. These principles are listed below (OECD, 2003):

1. Legal protection of shareholders (their right to dividends, being recipients of information, right to participate in the vote, the General Assembly, the right to monitor stock options among others).
2. Take action for the benefit of the majority and foreign shareholders.

3. The parties' role and rights, including the role of suppliers, customers and employees in the company's employ, the role of adhering to national law, and the participation of parties' to management of business according to the law.

4. Information transparency and dissemination in timely manner (calculation of the current fiscal year, consistent monitoring of administrative staff and emergency services, and independent audit). Information of other firm factors such as the duties of the board of directors and the executive committee, members of the board, independent members, method of appointment and wages should also be clarified.

The guidelines provided above are broad and countries are therefore free to apply them as they deem fit. Some countries even stated that despite the fact that there is no intention to provide a more universal model of CG; standards are provided to satisfy global needs yet (Collier & Gregory, 1999).

CG covers stakeholders' relationships and the objectives for which the corporation is functioning. The principal shareholders include management and board of directors while others include employees, customers, creditors, suppliers, regulators and the community (Mahboob, 2006). Similarly, CG is defined as the relationship between corporate managers, directors, and the providers of equity, people and institutions who invest capital. Thus, CG can be described as the set of mechanisms that are set in place to oversee how the firms are managed and long-term shareholder value is enhanced (Boubakri, 2011).

Established on a comprehensive review of the literature on the prior definitions of CG, the present study agrees with the one provided by Santosh (2005) and Boubakri (2011) as explicated above. In other words, the present study agrees that CG refers to the structure and processes associated with the board of directors, shareholders, top management along with other stakeholders and the objectives of ensuring accountability and enhancement of performance.

3.3.2 Corporate Governance Importance

CG has garnered significant attention in the circles of academics and business practitioners in the previous years, which resulted in the development and eventual laying down of codes of practice, conceptual models and empirical studies (Lazarri *et al.*, 2001). Proponents of CG claim that the stock price collapse, experienced by some US firms, including Adelphia, Enron, Parmalat, Tyco and WorldCom was because of poor governance (Gompers, Ishii & Metrick, 2003; Chaghadari, 2011). In Continental Europe, cases of Parmalat and Maxwell were attributed to inefficient hierarchy, such as top management teams, CEOs, and chairperson resulting in a sudden financial crisis (Clarke, 1998; Petra, 2005; Rose, 2006; Sussland, 2005).

CG is a critical effort that guarantees accountability and responsibility and a set of principles that has to be integrated into the firm's every department. CG has attracted a great deal of attention as it concentrates on the long-term relationship through checks and balances, incentives for managers and management-investors communications and most

importantly, transaction relationships involving disclosure and authority (Imam & Malik, 2007).

In the context of the US, CG committees have been set up particularly following the enactment of the Sarbanes Oxley Act (SOA) in 2001. These committees are aimed at promoting and driving companies to employ the best governance practices in their business and management. Similarly, in the UK, Cadbury in 1992 has structured CG to assist in the reduction of the conflict of interest between owners and managers and subsequently indirectly impacted companies' performance.

The presence of the CG committee improves the monitoring and supervisory role of the board over top management and executives. It provides new initiatives towards improving the boardrooms' governance structure and activities. As for director's remuneration, the CG committee ensures that the director is being remunerated on the basis of good performance (Najjar, 2012).

The premise of CG originally stems from the agency theory which covers investors, shareholder, manager, administrator and issues occurring as well as the issues attributed to the relations between those who are directly and indirectly associated to the company's affairs (Darwish, 2007). In the past century, CG has developed and led to attracting interests and debates (Abbott, Park & Parker, 2000). Moreover, the increasing corporate frauds and failures added to the CG interest and forced company directors, accounting

regulations, auditors, and in general the accounting profession into the limelight (Abbott, Park & Parker, 2004).

Moreover, according to Shleifer and Vishny (1997), CG involves the methods in which finance suppliers ensure that they will get a return on their investment. Similarly, John and Senbet (1998) involve all the stakeholders in the firm, and according to them it is a mechanism through which stakeholders take control over corporate insiders and management in a way that their interests are safeguarded.

CG literature in both developing and developed markets reveal that the roles of a regulatory authority, board, management, suppliers, customers and creditors are critical in enhancing the firm value. In the same way, Tricker (1994) described CG as an umbrella covering particular issues from interactions between senior management, shareholders, board of directors and other firm stakeholders. This is also consistent with Claudiu and Catalin's (2007) statement that CG has a key role in improving market confidence in the company and resulting in the company's prosperity and stability.

Related to agency problems, CG is a concept that is based on the agency theory, which is expected to serve as a tool to give confidence to investors that they will receive a return on the funds they have invested. CG is also related to how an investor can control or monitor the managers. Generally, management will seek to minimise agency cost, because higher costs would reduce the compensation offered to them (Herly & Sisnuhadi, 2011). Therefore, agency theory postulates that CG is a mechanism that minimises

conflicts through the monitoring of management performance and making sure that management's goals are aligned with that of other stakeholders (Brickley, Coles & Terry, 1994).

Likewise, Imam and Malik (2007) and Khan *et al.* (2011) claimed that the necessity for CG stems out from the possible conflicts of interest among stakeholders making the corporate structure – conflicts that are often attributed to two reasons; first, various participants have various goals and preferences and second, participants' own asymmetric information of each other's actions, knowledge and preferences.

Effective CG concentrates on the shareholders' interests and plays a key role in developing capital markets by safeguarding these interests (Abdurrouf, 2011). Obviously, good CG practices are increasingly essential in determining the cost of capital in a capitalist market.

Additionally, CG is a crucial ingredient of the firm performance and the development of the country's economy (Brava, Jiangb, Partnoyc & Thomasd, 2006; Ibrahim *et al.*, 2010). Theoretically, good CG should be linked to high corporate valuation. Several studies showed that investors are more inclined to a pay premium that averages at 10 to 12% for effective CG (Khanchel, 2007).

In the same vein, perfect CG can strengthen intra-company control and can reduce opportunistic behaviours and lower the asymmetry of information, so it positively affects the high quality information disclosure (Li & Qi, 2008). Furthermore, consistent with

Magdi and Nadereh (2002), CG ensures that business is being run properly and investors are recipients of a fair return.

Practically, CG and monitoring mechanisms are currently concentrating on issues concerning board composition, duties and responsibilities of the executive directors, consistent monitoring by shareholders, anti-takeover mechanisms, voting rights of shareholders and detailed disclosure of company information that are critical for decision making of the relevant parties. The framework of CG is described as a wide range control mechanism, internally and externally, to encourage the use of corporate assets and to require accountability for the resource stewardship. The CG challenge could result in aligning the individuals', corporations' and societal interests through a basic ethical basis and fulfilment of owners' long-term strategic goals. In turn, this may further lead to the development of shareholder value, establishment of dominant market share and sustenance of technical lead in a particular sphere. While this might be the case for all organisations, it will take into consideration the expectations of all the important stakeholders through the following; keeping in mind the interests of employees, customers and suppliers, debt holders, stockholders, local and state communities, in light of the physical effects of the company's operations and the economic and cultural interaction of the whole population. Hence, the maintenance of proper compliance with the legal and regulatory requirements under which the company's activities are built upon is another consequence of good corporate governance.

CG also ensures the equal treatment of the entire shareholders with the inclusion of minorities and foreign shareholders. The former group needs protection from abusive actions or illegal direct or indirect control. Stakeholders such as individual employees and their representative bodies should also be allowed to communicate freely regarding illegal and unethical practices to the board and their rights should be supported in doing so. Another CG responsibility is the timely and accurate disclosure of information relating to the firm. Information should be prepared and disseminated according to high quality standards of accounting and financial as well as non-financial disclosure. Members of the board should base their actions on the right information, in good faith, with due diligence and care and in the best interests of the shareholders. It is the responsibility of the board to employ high ethical standards and to commit effectively to their responsibilities (Imam & Malik, 2007).

Hence, good CG should be at the core of the organisation as this would reflect the organisational culture. Commitment to the principles of good corporate governance fosters investor confidence and attracts both domestic and foreign investors. Unfortunately, for Oman, it is lacking in these aspects. Currently, the Securities and Exchange Commission (SEC) expends efforts to encourage listed companies to adhere with the corporate governance rules and regulations in order to ensure that suppliers of funds get a return on their investment. If any infringement is noted, listed companies are required to provide justifications.

Finally yet importantly, a major portion of the literature indicates that the application of good CG requires properties that are credible and transparent in communication and information as the following Figure 3.1 illustrates:

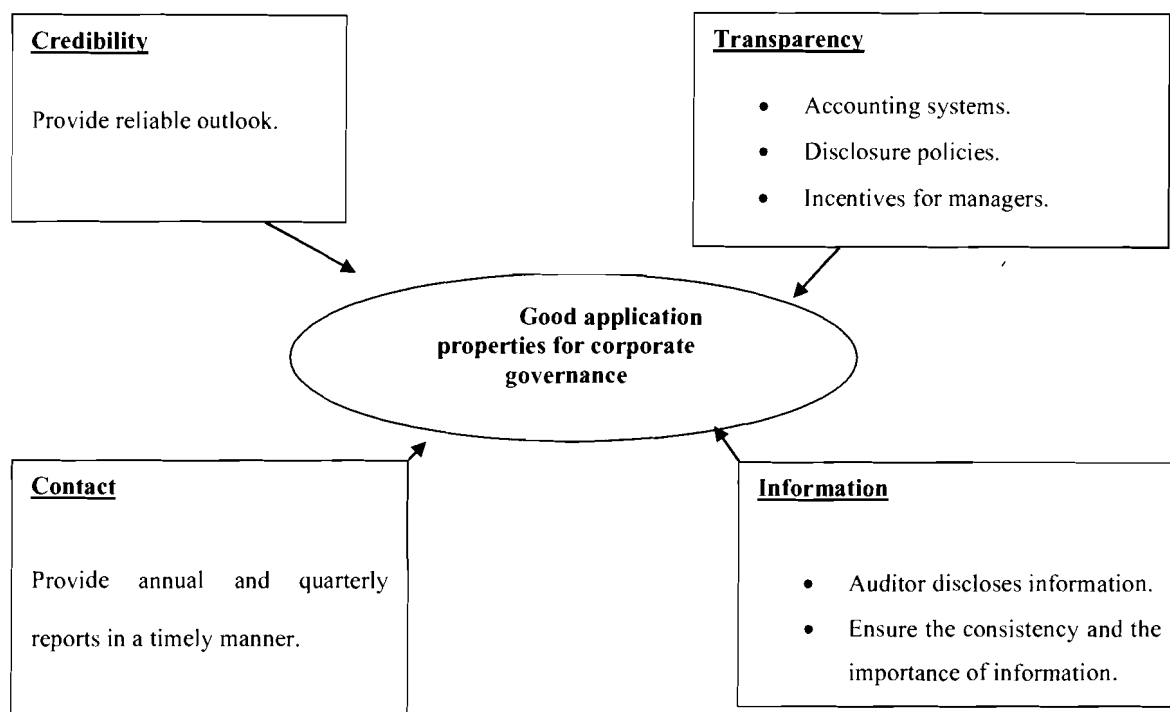


Figure 3.1
The Good Application Properties for Corporate Governance
 Source: Nuri and Salman (2010)

3.4 Corporate Governance and Firm Performance

Earlier studies that examined the relationship between CG and firm performance included Berle and Means (1932), Fama and Jensen (1983), Jensen and Meckling (1976), Shleifer and Vishny (1997) and Smith (1776). They found the importance of the splitting up of ownership and management in improving firm performance and providing confidence to

shareholders. Generally, they suggest that the separation between ownership and management will give managers freedom to make the right decision at the time. It offers motivations for managers to maintain firms' possessions in a manner that positively affects the wealth of shareholder and improve health of shareholders as well.

Literature, dedicated to CG sheds some light on various mechanisms that are available to shareholders to make sure that managers' actions are aligned with shareholders' interests. These are categorised into internal mechanisms with the former including board of directors, board independence and audit committee, while the latter including CEO, independent member and others. Nevertheless, the majority of studies concerning CG primarily focus on specific elements of governance such as board of directors, board independence, audit committee, CEO duality and others. Additional to the above, most studies investigated the association between CG and firm performance directly without moderators and mediators.

CG has always had to depend on the internal monitors to achieve an alignment between management and shareholders' goals (Pissaris *et al.*, 2010). Similarly, Cremers and Nair (2005) stated that CG may be internal and it plays a key role in improving the firm value and performance.

Moreover, the internal governance mechanism is employed by shareholders to guarantee that their goals are aligned with that of management's (Walsh & Seward, 1990). Therefore, internal mechanisms depend on the effective structure of the board, suitable

CEO compensation packages, and concentrated ownership to facilitate active monitoring (Pissaris *et al.*, 2010). Practically, two significant forms of governance system have been developed for huge corporations in economic and financial literature, i.e. the Anglo-American type (outsider system) and the Japanese-German type (insider system).

Although the application of CG code has been executed for a long time in the developed countries and many works have been performed in this context; the results are still conflicting and unconfirmed with various recommendations. In this scenario, it is easy to imagine the situation in underdeveloped countries, which are still suffering how to split up management and ownership, and where there is a great need to study the relationship between governance and performance. This justifies the goal of the current study, which is to study the relationship between CG and firm performance in firms of one of the developing countries (Al-Matari *et al.*, 2012a; Al-Matari *et al.*, 2012).

The importance of CG was recognised after financial crisis, which hit the economy of the developed countries such as US, UK, Australia and others in the early 1990s. The government of the developed countries tried to set some rules and regulations in the form of CG to clarify the relationship between owners and managers. The main target of this code is to attract investors, both local and foreign, and to protect the value of shareholders.

As previously mentioned, there are numerous scholars who have explored the relationship between CG and firm performance in the developed countries (e.g.

Galbreath, 2010; García-Sánchez, 2010; Larmou & Vafeas, 2010; Millet-Reyes & Zhao, 2010; Nanka-Bruce, 2011; O'Connell & Cramer, 2010; Reddy *et al.*, 2010; Stanwick & Stanwick, 2010; Sueyoshi *et al.*, 2010). They took a long time to identify the best practices of corporate governance. But in the developing countries, the situation is different concerning the study of the association between CG and firm performance precipitated by the Asian financial crisis. Given the importance of best practice of CG in encouraging investors to invest their money in a country, there is a dire need to investigate this relation in the emerging market. Moreover, there are many studies that are recommended to observe the association between CG and firm performance in the developing countries (Adeyemi & Fagbemi, 2010; Al-Matari *et al.*, 2012a; Al-Matari *et al.*, 2012; Gibson, 2003; Jackling & Johl, 2009; Joher & Ali, 2005; Lin, Ma & Su, 2002).

As mentioned above, the issue of CG has emerged as an important phenomenon that has been searched extensively in developed countries due to its strategic impact on the monitoring of management activities and firms' performance. Yet little attempt has been made in developing countries in general, particularly in Oman, to ascertain what constitutes CG and its impact on the firm's performance. Therefore, this study aims to examine the structure of the CG and its impact on the firm's performance. This study also intends to bridge the gap through the addition of new variables to firm performance. Additionally, the current study focuses on both internal and external variables of CG and it examines if the change to study some moderator and mediator variables between CG and performance.

A look at the literature reveals that most of the research on CG and performance is directly focused to examine the relationship between the level of corporate governance and various aspects of firm performance. This study stands out as it utilises a set of governance variables providing an extensive picture of the company and industry level governance practices along with international standard mechanisms and the board structure. This is explained in the next section.

The study includes new variables such as, the change board, the role of secretary on the board, the legal counsel, foreign member on the board and the executive committee. Moreover, this study has used many variables such as firm size, leverage, industry and time period as control variables.

Although there have been many studies that examined the association between factors of corporate governance and firm performance in both the developed and developing countries in the past two decades, but these studies focused on separate variables as mentioned earlier in the significance of the study in Chapter One. Many recommend variables of firm performance, such as Adeyemi and Fagbemi (2010), Al-Matari *et al.* (2012a), Azam *et al.* (2011), Belkhir (2005), Khan and Javid (2011), Khan *et al.* (2011) and Valenti *et al.* (2011), where the majority of them studied board characteristics, CEO duality and some factors of committees with firm performance.

A thorough review of the current literature pertaining to CG and firm performance reveals the following two issues:

Firstly, empirically prior literature on the relationship between CG and firm performance is extensive in the developed countries, but there is a limited study in the developing countries. However, the findings are inconclusive. One literature stream finds that CG is positively associated with firm performance (e.g. Azam *et al.*, 2011; Bozcuk, 2011; Bozec *et al.*, 2010; Chahine & Safieddine, 2011; Chamberlain, 2010; Ghahroudi, 2011; Ibrahim & Abdul Samad, 2011; Heenetigala & Armstrong, 2011; Kang & Kim, 2011; Khan, Nemati & Iftikhar, 2011; Khatab *et al.*, 2011; Larmou & Vafeas, 2010; Leung & Horwitz, 2010; Mahadeo *et al.*, 2012; Najid & Abdul Rahman, 2011; Obiyo & Lenee, 2011; Pissaris *et al.*, 2010; Reddy *et al.*, 2010; Shahab-u-Din & Javid, 2011; Stanwick & Stanwick, 2010; Sueyoshi *et al.*, 2010; Swamy, 2011; Uwuigbe & Olusanmi, 2012). Conversely, other studies demonstrate a negative relationship between CG and firm performance (e.g. Evans *et al.*, 2010; Garcí'a-Meca & Sa'nchez-Ballesta, 2011; Herly & Sisnuhadi, 2011; Muravyev *et al.*, 2010; Rachdi & Ameer, 2011; Roselina, 2009; Switzer & Tangb, 2009; Valenti *et al.*, 2011; Wang & Oliver, 2009). In addition, some researchers found no relationship between CG and firm performance (e.g. Bhagat *et al.*, 2011; Chowdhury, 2010; Gibson, 2003; Herri, 2011; Kiel & Nicholson, 2006; Shao, 2010; Wei, 2007).

Secondly, there has been a lack of comprehensive study generally in emerging market and specifically in Oman to investigate factors of CG including internal and external variables.

3.5 Board of Directors Characteristics and Firm Performance

In this section, some mechanisms that play a vital role in board characteristics such as: board size, board independence and board meeting are discussed. These variables are very important in reflecting the performance of firms in the developing countries (Nuryanah & Islam, 2011; Young, Peng, Ahlstrom, Bruton & Jiang, 2008). Based on the prior studies concerning the association between board characteristics and firm performance, the findings are still inconclusive. It is also evident that no study (to the knowledge of the researcher) has investigated any variable between CG and firm performance. The current study is the pioneering study to add some variables to the board structure, including board changes, the role of secretary on the board and legal counsel. Moreover, it includes new variables to the corporate structure, including the executive committee. Furthermore, there is lacking in previous studies to examine foreign member of the board with firm performance. Thus, this study investigates the relationship between foreign member on the board and firm performance.

As a result, these variations are essential for enhancing performance, providing new insight and innovation. In the end, the next part reviews board characteristics, namely, board size, board independence and board meeting. Due to the above explanation in the first chapter on weaknesses and severe shortages of relevant literature, companies have been trying to improve the performance by improving the application of CG in the Omani companies. This study tries its best to bridge the gap in previous studies by examining some of the factors that are very important to improve and develop the application of CG

in the Omani companies and eventually to enhance corporate performance. Resultantly, attracting new investors will help the country's economy to prosper. Therefore, it is very useful to add some variables to the board of director's characteristics such as board change, the role of secretary on the board and the legal counsel as follows:

3.5.1 Board Size and Firm Performance

The first important board of director's characteristic is the board size. It has also, along with its effect upon board effectiveness, been extensively studied (Jensen, 1993). The board size refers to the number of directors on the board (Al Manaseer *et al.*, 2012; Nanka-Bruce, 2011; O'Connell & Cramer, 2010; Rachdi & Ameer, 2011). The board of directors is the main internal governance mechanism responsible for monitoring executive decisions (Al Manaseer *et al.*, 2012).

The board represents a group of elected people or those who are appointed by the owners of a company to jointly oversee the activities of the company. Besides, board members (directors) may be or not be owners and managers. Board members who are owners or managers are sometimes referred to as internal or executive directors, while board members who are not owners or managers are sometimes referred to as external or independent directors (Shao, 2010). Moreover, the existence of the board of directors is not only because state incorporation laws mandated firms to keep one, but also because the board is an effective market solution to an issue of organisational design as it plays the role of resolving the contracting issue within organisations (Bozec, 2005).

The effectiveness of CG practice is a function of the board where it has a vital role to play in a company, as its function is to manage and direct the management (Farrar, 2005; Nuryanah & Islam, 2011). It also plays a monitoring role since a separation exists between ownership and control within the company (Jensen & Meckling, 1976). Likewise, the board is also core to CG mechanisms and is considered as the main mechanism that shareholders can employ to control top management (John & Senbet, 1998).

The board is responsible for determining the overall strategy of the firm, and to assure sufficient administration for the protection of the shareholder value (Keenan, 2004). Practically, corporate boards allocate most of their duties to the management team, but hold the authority to hire, to compensate, and if needed to replace top executives (Fama & Jensen, 1983). The main responsibility of corporate decisions still remains with the board and it has a fiduciary duty to make sure that the firm is capable of withstanding any critical business conditions affecting its performance.

Fama and Jensen (1983) added that the board of directors should comprise of both external and internal directors. Internal directors have technical competencies and relevant knowledge of the firm, while external directors contribute to carrying out strategic decisions and they provide more effective management monitoring compared to internal directors (Chahine & Safieddine, 2011). In the same context, in the emerging markets, the board becomes important tool complementing for the inefficient external CG mechanisms to alleviate conflict of interests amongst parties. Consistent with the above

arguments, the board of directors is a main structural mechanism that minimises opportunistic activities. As a control mechanism, the board is responsible to represent and defend the interests of the shareholders against managerial entrenchment (Nuryanah & Islam, 2011; Young *et al.*, 2008).

In Oman, owing to the majority internal members of the board of directors, the authority enumerates points that are directed to achieve the firm's targets and aims. These roles help firms to protect shareholder wealth. Regarding to Omani CG code, board of directors has the following roles (Oman Code of CG, 2002):

1. Providing approval for the company business and financial policy to achieve the objectives and to increase shareholders' value.
2. Revising and providing approval for the financial objectives, plans and activities.
3. Providing approval for the internal regulations of the company concerning routine activities and laying down the responsibilities and the authorities of the executive management.
4. Laying down the disclosure policy of the company and overseeing the compliance with the regulatory requirements.
5. Providing their approval of delegating power to the executive management, the delegation of power involves the specification of the level of approving authority and the methods of tendering with suitable limits. The situations under which tender

(other than the lowest one) is acceptable are clearly laid down. Management should note down the reasons in writing for overlooking the lowest bid.

6. Conducting a review of the company's performance in order to evaluate if the business is managed properly as per the company's objective and guaranteeing adherence to the laws and regulations through proper internal control mechanisms.
7. Conducting a review of material transactions with the relevant party and to bring forth the same issue before the company's general meeting.
8. Reviewing the performance of the company in order to analyse whether the business is managed in a proper manner.
9. Nominating the sub-committees' members and clarifying their roles, responsibilities and authorities.
10. Selecting the CEO or General Manager and other executives and clarifying their roles, responsibilities and authorities.
11. Analysing the functions of the key employees, the CEO and the sub-committees.
12. Providing approval of the interim and annual financial statements.
13. Keeping the shareholders in the loop, the status of the company and providing supporting assumptions and qualifications if needed.

Prior studies have reviewed the relationship between board size and firm performance. Largely, prior investigation on the relationship between board size and firm performance provided an extensive explanation of the relationship between them. With regards to agency theory, there are number of finding. However, this study is unique and different as compared to the previous studies. It takes separate associations that are consistent with theories. For example, the first section highlights the first theory and provides studies to support the theory. The second section discusses the second theory and supports the theory with studies from the literature. In general, many studies on a global scale have investigated the relationship between board directors' size and firm performance although the findings are still inconclusive.

This section sheds light on agency theory as mentioned above. Under the agency theory, the agency proponents argue that a board of smaller size with minimised monitoring duties encourage efficiency, strategic discussions, coordination and communication. With the increase in board size, conflicts of interest arise in decision-making and the majority of the members resort to becoming lazy and passive in their duties of providing resources (Abdurrouf, 2011; Jensen, 1993; Nanka-Bruce, 2011). In the same context, as Yermack (1996) stated, issues of communication, coordination and decision making hinder company performance with the increase in the number of directors. Hence, an additional member should be included on the board, a possible trade-off existing between coordination and diversity.

Jensen's (1993) statement is consistent with Lipton and Lorsch's (1992) who suggested an ideal number of board members to be seven or eight. In the same way, Firstenberg and Malkiel (1994) claimed that a board having eight or less members maintains greater focus, participation, authentic interaction and debate. Consistent with Shaver's (2005), larger boards generally show diffusion of responsibility, encouraging social loafing, group fractionalisation, and minimisation of strategic change commitment.

In empirical studies consistent with the agency theory, there are many researchers around the world who have investigated the relationship between board size and firm performance and they found a negative relationship between board size and firm performance in the developed countries such as Ben-Amar and Andre (2006), Florackis (2005), Gavrea & Stegorean (2012), Irina and Nadezhda (2009), Juras and Hinson (2008), Liang, Xu, & Jiraporn (2013), Nanka-Bruce (2011), O'Connell and Cramer (2010) and Yawson (2006). On the same path, in the developing countries, the relationship between the board size and firm performance has been found to be negative (Al Farooque, Zijl, Dunstan, Karim, 2007; Al Manaseer *et al.*, 2012; Ali & Nasir, 2014; Al-Najjar, 2014; Amran & Che-Ahmad, 2009; Chechet, Jnr & Akanet, 2013; Garg, 2007; Haniffa & Hudaib, 2006; Ibrahim & Abdul Samad, 2011; Kota & Tomar, 2010; Lin, 2011; Mashayekhi & Bazazb, 2008; MoIlah & Talukda, 2007). Finally, for extensive information, refer to Table 3.1 in Appendix A.

This section explains another theory that relates to the company's performance known as the resource dependence theory and it relates to board directors' size. The firm board size

has received increasing attention, especially considering the failures of prominent businesses. The more number of board members, the more relations to the external environment exist to gather critical resources and information for decision making on corporate policies that will improve efficiency (Goodstein, Gautam & Boeker, 1994; Nanka-Bruce, 2011).

In the same context, Chaganti, Mahajan and Sharma (1985) and Dalton, Daily, Ellstrand and Johnson (1998) stated that large boards are invaluable as the members to the board decision making contribute diverse experiences. They recommend that a larger board is more effective compared to a smaller one in steering clear of corporate failure (Dallas, 2001). Another school of thought possesses the same opinion and is convinced that firms having larger boards are able to urge managers to decrease costs of debt and increase performance (Anderson, Mansi & Reeb, 2004).

To guarantee board's execution of duties, members of the board should be prepared to commit significant resources and to offer various skills. It comes to reasonable argument that a larger board size is invaluable to the efficient firm performance, as more board members would translate to more information sources varied opinions available to a firm (Ghabayen, 2012).

A larger board is also associated with stricter monitoring of management to guarantee minimisation of financial fraud. Nevertheless, the advantages of having larger board size may be outweighed by its costs because it may be challenging for a larger board to

achieve a consensus indicating that smaller boards could lead to minimised coordination problems and enhanced efficiency performance. Moreover, the large board size may indirectly lead to free-rider issues or low motivation among the members of the board (Hsu & Petchsakulwong, 2010).

Additionally, Brown and Caylor (2006) stated that a board size, comprising of 15 members is sufficient for large firms, as if it goes beyond this more free-riding issue will increase and some directors may forget to fulfil their duties of monitoring and resource provision. They recommend a board size of 6 to 15 members to be the ideal size in enhancing firm performance. Consistent to Adams and Mehran's (2003) and Uadiale's (2010) argument, board size suggestions are bound to be industry-specific as bank holding companies have larger board size compared to manufacturing companies. Moreover, Abor (2007) and Wen, Rwegasira, Bilderbeek and (2002) claimed that large boards have the effective ability to monitor and pursue higher standards in raising firm value.

According to the resource dependence theory, the board's function is to acquire firm resources based on the relationships between the board members and other organisations (Pfeffer, 1972; Provan, 1980; Zald, 1967). The acquisition of these resources enables the board members to minimise the degree of environmental uncertainty of the firm (Burt, 1983; Pfeffer, 1972; Thompson, 1967). The board is responsible for assisting in maintaining the organisation's legitimacy and creating a boundary of opportunities in the expectations of aligning the firm's interests with other firms' (Dooley, 1969; Pennings,

1980). The board is also responsible for contributing valuable input to the way strategic decisions are conducted by the firm (Westphal & Fredrickson, 2001).

Along a similar line of argument, the theory adds that larger board size would result in enhancing company performance owing to the various skills, knowledge, and expertise provided to the boardroom discussion. Large boards are able to offer the diversity that could assist companies to obtain critical resources and minimise environmental risks (Goodstein *et al.*, 1994; Ghazali, 2010; Pearce & Zahra, 1992; Pfeffer, 1987).

Based on the discussions above concerning the importance and the role of the large size of the board, the current section mentions empirical studies around the world to support that large board size to promote and improve firm performance. Hence, the relationship between board size and firm performance is positive, according to the resource dependence theory perspective. There are many researchers in the developed countries who found a positive association between these two (Bauer *et al.*, 2009; Fairchild & Li, 2005; Galbreath, 2010; Juras & Hinson, 2008; Khanchel, 2007; Larmou & Vafeas, 2010; Lee, 2009; Premuroso & Bhattacharya, 2007; Sueyoshi *et al.*, 2010). In the same context, there are also authors in the developing countries who found this outcome, such as, Abdullah *et al.* (2008), Al-Najjar (2013), Black, Jang and Kim (2003), Chahine and Safieddine (2011), Chugh, Meador and Kumar (2011), Danoshana and Ravivathani (2014), Dar, Naseem, Rehman and Niazi (2011), Dwivedi and Jain (2005), Ehikioya (2009), Haniffa and Hudaib (2006), Hsu and Petchsakulwong (2010), Ibrahim *et al.* (2010), Jackling and Johl (2009), Kajola (2008), Kamardin (2009), Kang and Kim

(2011), Khan and Javid (2011), Kyereboah-Coleman and Biekpe (2006), Li, Kankpang and Okonkwo (2012), Mehraban and Dadgar (2013), Najjar (2012), Obiyo and Lenee (2011), Sahu and Manna (2013), Saibaba and Ansari (2013), Sheikh, Wang and Khan (2013), Swamy (2011), Uadiale (2010), Yasser, Entebang and Mansor (2011) and Zainal Abidin, Kamal and Jusoff (2009). For extensive information, refer to the Table 3.2 in Appendix A.

Finally, this section provides empirical studies who found no relationship (not significant) between board size and firm performance whether in developed countries (Abdurrouf, 2011; Aljifri & Moustafa, 2007; Al-Matari et al., 2012; Al-Matari et al., 2012b; Al-Najjar, 2013; Bektas & Kaymak, 2009; Belkhir, 2005; Chaghadari, 2011; Chiang & Lin, 2011, Dar, Naseem, Rehman & Niazi, 2011; Ghabayen, 2012; Ghazali, 2010; Guoa & Kgab, 2012; Ibrahim & Abdul Samad, 2011; Ibrahim et al., 2010; Kajola, 2008; Kamardin, 2009; Kiel & Nicholso, 2006; Kula 2005; Kyereboah-Coleman, 2007; Kyereboah-Coleman & Biekpe, 2006; Latief, Raza & Gillani, 2014; Lin, 2011; Noor, 2011; Nuryanah & Islam, 2011; Prabowo & Simpson, 2011; Rachdi & Ameer, 2011; Stanwick & Stanwick, 2010; Vo & Nguyen, 2014). For more information, please refer to the Table 3.3 in Appendix A.

3.5.2 Board Independence and Firm Performance

Board independence is another measure of board characteristics quality at the board level that has garnered significant attention. Generally, board independence is a critical

element of CG that contributes to overseeing firm performance as several studies have evidenced (Adjaoud, Zeghal & Andaleeb, 2007; Koufopoulos *et al.*, 2008). Board independence is described as the number of independent non-executive directors having a seat on the board relative to the total number of directors (Lawal, 2012; Uadiale, 2010). An independent non-executive director refers to an independent director having no affiliation with the firm other than directorship (Clifford & Evans, 1997).

Several corporate charters mandate that the shareholders elect the board of directors whose responsibility include monitoring, management and assisting in the firm's strategic planning. More specifically, for the effective execution of management monitoring, it is important that the board should work independent of management (Belkhir, 2005). Therefore, a number of academicians and professionals are of the consensus that the directors who are not employees of the firm may help in improving the effectiveness of the board of directors in their overseeing duties and in enhancing firm value. The justification behind this notion is that external directors are more likely to advocate for the external shareholders' interests (Belkhir, 2005).

In addition, regarding to an Omani Code of Corporate Governance (2002) that the board has to have at least three persons is non-executive – specifically, the board should comprise of a majority of non-executive directors as board independence plays a key role in monitoring (Lin, 2011).

Therefore, the primary role of independent directors is to monitor and control firm activities in an effective manner in an attempt to minimise the managerial opportunistic behaviours and expropriation of firm resources (Abdurrouf, 2011; Pandya, 2011). As the board of directors is the most significant mechanism that monitors management, independence of the members is a critical issue (Abdullah, 2004; Chaghadari, 2011).

External directors refer to those individuals who are not employed by the company or by any affiliated companies. They do not offer consulting services to the company's management, and are not recipients of any income from the company or from the relatives of the executives working for the company. Some studies have investigated the effect of cross-board representation (one director sitting on several board seats) upon performance (Fich & Shivdasani 2006; Irina & Nadezhda, 2009).

Board independence is the level to which board members do not depend on the CEO/Management owing to its composition. External board members are not involved in the daily firm operations, but they are more likely to cogitate more independent when it comes to the performance of the firm. Moreover, their experiences assist in generating novel perspectives and ideas regarding earning performance (Swamy, 2011). Sharing the same thought, the principal role of non-executive directors is to protect shareholders' interests when the company makes decisions (Fernandes, 2008).

External board members are also more persistent in their monitoring role as they are responsible for guaranteeing strong financial performance (Johnson, Hoskisson & Hitt

1993; Stanwick & Stanwick, 2010). Along the same line, independent directors seated on the board are free to work and are not subjected to get controlled or influenced by the major shareholders, management or other relevant parties or from all three. They are also more likely to monitor management's fraudulent activities, as they do not have any economic or psychological relationship with management (Hsu & Petchsakulwong, 2010).

Additionally, the independent board serves as a monitoring device to control management activities. The board independence usually requires that members are not closely related to the company but have vested economics or financial interest on the firm's residuals. Hence, this could be further argued that such independent board members can significantly contribute to decision making of the board by bringing more objective view to the evaluation of the performance of the board management. Though the depth of directors' independence is more formal than substantial, the percentage of independent directors on the board is still relatively minor in most of the developing countries (Joher & Ali, 2005).

Furthermore, Fama and Jensen (1983) claimed that external directors have the reputations and social status, which work as incentives in monitoring management and ensuring the effective running of the company. The board independence also assists in reducing agency problem that shareholders should request to replace internal directors by external ones to achieve effective management monitoring (Hermalin; Weisbach, 1991; Weisbach, 1988).

On the same token, Daily (1995) argued that external directors offer a more effective level of objectivity when assessing the firm's situation. Similarly, Coughlan and Schmidt (1985) contended that external directors are more effective when monitoring and acting as a disciplining mechanism for managers.

All CG practices around the world suggest that an independent member should be included on the board (Nuryanah & Islam, 2011). In the same path, independent directors minimise the agency cost as they make the monitoring role and the strategic planning role of the board more effective (Berle & Means, 1932). Considered as an important attribute of a good board, Oman in its CG practice suggests that every listed company should have at least 30% of its board independent members as mentioned above.

Consistent with the above, Uadiale (2010) recommended that the composition of external directors as members of the board should be maintained and enhanced in order to improve the financial performance of the firm. Choi, Park and Yoo (2007) also supported this contention by stating that the presence of external directors might be good for the performance of the firm as it contributes to external monitoring and independent market discipline. Similarly, Shivdasani (2004) claimed that board independence is impacted by the decrease in financial performance as companies react to digressing performance by nominating external directors to the board who are inclined to take disciplinary actions such as replacing the CEO.

In the same context, Koufopoulos *et al.* (2008) and Young, Stedham and Beekun (2000) revealed that external board members offer more to board's independence and are more dedicated to holding the CEO accountable for their performance by adopting a formal process of evaluation. Empirically, many researchers around the world have examined the relationship between board independence and firm performance, whether in developed nations or the developing states. However, there is no consensus on specific results and the findings are still mixed. These results are discussed in the next section. Theoretically, under the agency theory perspective (monitoring) and resource dependence theory (the provision of resources), a greater proportion of external directors on the board translates to independent monitoring in circumstances where a conflict of interest between management and shareholders arises.

The agency theory is based upon the notion that an inherent conflict exists between the interests of the firm's owner and its manager (Fama & Jensen, 1983). With regards to corporate governance, the agency theory indicates that sufficient monitoring mechanisms should be laid down to safeguard shareholders from management's selfish behaviours. Thus, the majority of external directors on the board are considered to have a positive effect on performance (Fama & Jensen, 1983; Jensen & Meckling, 1976; Shleifer & Vishny, 1997).

Advocates of the agency theory are convinced that CG should result in higher stock prices or improved long-term performance as managers are being monitored effectively and agency costs are minimised. The theory postulates that the board should comprise of

the majority of non-executive directors, as a large number of independent directors can offer effective monitoring of manager's actions so that shareholders' interests are safeguarded and they may reap greater returns (Nicholson & Kiel, 2007). Compared to their internal counterparts, independent directors are more effective in monitoring firm management owing to their separation from the firm and the CEO (Johnson, Daily & Ellstrand, 1996).

Consistent to resource dependence theory, the external sources provide a firm with external channel to improve performance of the company. Moreover, an independent board allows board members to comprehend complex environments, give multiple knowledge and experience from different sources, and in turn improve firm performance (Pfeffer, 1972). In other words, an independent board provides a firm with multiple resources to help in making the right decision.

The above discussion concerning agency theory and resource dependence theory indicates that both the theories support the contention that the company should have more board independence to achieve improved performance. Hence, the relationship between the independent board and firm performance should be positive. In this section, studies dedicated to the investigation of the relationship between board independence and firm performance in developed states and from developing countries are discussed.

Studies investigating the relationship between board independence and firm performance in developed countries reveal a positive association. Many researchers carried out studies

regarding this relationship in the developed countries such as Adjaoud *et al.* (2007), Bhagat and Bolton (2009), Bozec *et al.* (2010), Chamberlain (2010), Cordeiro, Veliyath and Romal (2007), Dey (2008), Filatotchev, Isachenkova and Mickiewicz (2007), Florackis (2005), Galbreath (2010), Harjoto and Jo (2008), Heenetigala and Armstrong (2011), Juras and Hinson (2008), Khanchel (2007), Lehn, Patro and Zhao (2009), Liang, Xu, and Jiraporn (2013), Lin, Hu (2002), Mahadeo *et al.* (2012), Müller (2014), Mura (2007), Nanka-Bruce (2011), O'Connell and Cramer (2010), Premuroso and Bhattachar (2007), Reddy *et al.* (2010), Saibaba and Ansari (2011), Shan and McIver (2011) and Yawson (2006). Moreover, there are also many researchers in the developing countries who revealed a positive relationship between the board independence and firm performance such as Azam *et al.* (2011), Black and Kim (2007), Black *et al.* (2003), Bozcuk (2011), Chiang and Lin (2011), Cho and Kim (2007), Choi *et al.* (2007), Filatotchev, Lien and Piesse (2005), Hsu and Petchsakulwong (2010), Hsu *et al.* (2009), Jackling and Johl (2009), Kamardin (2009), Khan *et al.* (2011), Kula (2005), Kyereboah-Coleman (2007), Kyereboah-Coleman and Biekpe (2006), Mashayekhi and Bazazb(2008), Nuryanah and Islam (2011), Uadiale (2010) and Zainal Abidin, Kamal and Jusoff (2009). For more information, refer to the Table 3.4 in Appendix A.

Contrary to the agency theory and the resource dependence theory, many empirical evidences around the world found a negative association between the board independence and firm performance. First, a negative relationship between board independence and firm performance was revealed in developed countries, Bhagat and Bolton (2008), Bozec

(2005), Firth, Fung and Rui (2006), Irina and Nadezhda (2009), Jermias and Gani (2014), Pan, Lin and Chen (2013), Singh and Gaur (2009), Stanwick and Stanwick (2010), Switzer and Tangb (2009), Valenti *et al.* (2011) and Wang and Oliver (2009). Similarly, there is an identical finding in the developing countries as evidenced by Bektas and Kaymak (2009), Chahine and Safieddine (2011), Chang (2009), Ghabayen (2012), Khan and Javid (2011), Noor (2011), Sahu and Manna (2013), Sheikh, Wang and Khan (2013) and Vo and Nguyen (2014). For more details, please refer to the Table 3.5 in Appendix A.

Besides, there are some studies that investigated the relationship between board independence and firm performance and discovered no relationship (insignificant) between these two whether in the developed states such as Adjaoud *et al.* (2007), Bøhren and Strøm (2010), García-Sánchez (2010), Hu, Tam and Tan (2010), Siala *et al.* (2009), Wei (2007) and Yue, Lan and Jiang (2008) or developing nations like Abdullah (2004), Al-Matari *et al.* (2012), Al-Matari *et al.* (2012b), Chowdhury (2010), Chugh *et al.* (2011), Ehikioya (2009), Garg (2007), Ghazali (2010), Guoa and Kgab (2012), Haniffa and Hudaib (2006), Ibrahim and Abdul Samad (2011), Ibrahim *et al.* (2010), Kota and Tomar (2010), Kumar and Singh (2012), Kyereboah-Coleman (2007), Kyereboah-Coleman and Biekpe, (2006)Kyereboah-Coleman and Biekpe (2006), Latief, Raza and Gillani (2014), Leng (2004), Noor (2011), Pandya (2011), Prabowo and Simpson (2011), Rachdi and Ameer (2011) and Sahu and Manna (2013). For complete information, refer to the Table 3.6 in Appendix A.

3.5.3 Board Meeting and Firm Performance

This section provides one of the vital board characteristics, namely the board meeting. The board meeting represents the number of meetings the board has during a year. Regarding to the Omani Code of Corporate Governance (2002), the board should have a meeting at least 4 times a year with a maximum of 4 month gap between two meetings.

Prior studies have focused on studying two factors of board characteristics, i.e. board size and board independence, but the current study adds board meetings (Al Manaseer *et al.*, 2012; Kang & Kim, 2011; Li *et al.*, 2012; Nanka-Bruce, 2011; Obiyo & Lenee, 2011) as it has become so vital within the companies. Board meetings are important because boards act on the behalf of the company and there is a method where the board acts collectively namely the passing of a resolution on board meetings. More meeting means more chances of considering different decisions by the boards and quickly reaching to final results (Khan & Javid, 2011).

The board effectiveness is reflected through its meetings. The frequency of board meetings can lead to the improvement of the firm performance as frequent meetings translate to more opportunities to monitor and review the performance of management (Hsu & Petchsakulwong, 2010). Consistent with the above, Evans, Evans and Loh (2002) revealed that the board of directors often increase the frequency of board meetings if they have to solve issues concerning declining performance.

Along the same line, Jackling and Johl (2009) and Lipton and Lorsch (1992) claimed that the higher the frequency of meetings is, the more likely is the firm to perform better. In a similar contention, Conger, Lawler and Finegold (1998) and Kyereboah-Coleman (2007), stated that board meeting time is a critical resource for enhancing the corporate board's effectiveness. In other words, the above studies indicate that with frequent meetings, board of directors is likely to improve firm performance and perform their duties according to the interests of the shareholders.

Furthermore, based on Vafeas (2000) study, frequency of board meetings is crucial, since by increasing the frequency the board can contribute in enhancing the firm's operating performance. Therefore, the board should be ready to increase the frequency of their meetings when the circumstances call for strict supervision and control (Khanchel, 2007; Shivdasani & Zenner, 2002).

More importantly, the intensity of the board, measured by the frequency of its meetings is a crucial aspect of resource dependence theory associated with CG and performance. Regarding the resource dependence theory, the board meeting helps the board to evaluate and pursue a board matter in a timely manner and to solve any problems, which are faced by employees (Pearce & Zahra, 1992; Pfeffer, 1987). Hence, increased board meetings translate to increased performance of the firm.

Consistent with previous suggestions and the resource dependence theory as mentioned above, the relationship between board meetings and firm performance is expected to be

positive. There have been studies in various countries that found a positive association between board meetings and firm performance. This current study is unique as it discusses many studies done from developed countries and developing countries. The relationship between board meetings and firm performance is positive in developed countries (Gavrea & Stegorean, 2012; Khanchel, 2007; Liang, Xu, & Jiraporn, 2013; Lin *et al.*, 2002). On the other hand, there were some researchers who found that the relationship between board meetings and firm performance in the developing nations is positive such as, Hsu and Petchsakulwong (2010), Kamardin (2009), Kang and Kim (2011), Khan and Javid (2011) and Sahu and Manna (2013). For more information, refer to the Table 3.7 in Appendix A.

This study revises the perspective of the resource dependence theory as discussed above and verify it through the agency theory. The results declared by Jensen (1993) revealed that routine tasks occupy most of the board's meeting time and confine the chances for external directors to carry out meaningful control over management, although the same author suggested that boards should be relatively inactive as poor performance is reflected by higher board activity.

Additionally, Jackling and Johl (2009) suggested that increased board activity is a response to poor performance, which in turn is related to improve operating performance in the near future indicating the existence of a lag effect. On the other hand, Khanchel (2007) suggested that boards have to balance the frequency costs and benefits. Another point of the view came from Rebeiz and Salame (2006) who claimed that the board

meeting frequency is secondary to its quality. In other words, higher frequency of board meetings indicates that the board is playing an inappropriate operating role and the role of the board is managing the firm instead of governing the management.

Based on the above discussion, there is supposed to be a negative relationship between frequency of board meetings and firm performance. However, the studies revealing this negative relation in the developed and developing countries are limited. For instance, Danoshana and Ravivathani (2014), García-Sánchez (2010), Kamardin (2009), Noor (2011) and Qinghua, Pingxin and Junming (2007), showed that the frequency of board meetings-firm performance relationship is negative. For more details, refer to Table 3.8 in Appendix A.

Finally, beyond from the proponents and perspective of agency theory and resource dependence theory, researchers investigated the board meeting and firm performance in general. Their result revealed no relationship (insignificant) between the two (e.g. Gavrea & Stegorean, 2012; Kyereboah-Coleman, 2007; Noor, 2011). For more information, refer to Table 3.9 in Appendix A.

To conclude, this study has reviewed some dimensions of board characteristics, namely board size, board independence and board meeting whereas, almost all the prior studies examined the relationship between board characteristics and firm performance directly. Moreover, this study adds some new variables such as board change, the role of secretary on the board and foreign member on the board to the board of director characteristics. So,

this study examines the direct relationship between the board change and the role of secretary on the board and firm performance. In addition, this study investigates the relationship between the executive committee and firm performance. It is notable that no study (to the knowledge of the researcher) has ever been conducted to examine this association with reference to the Omani Code of Corporate Governance (2002). While these elements are really significant in enhancing performance of the firm, therefore this present subject is unique in itself owing to its distinction to other subjects.

3.5.4 Board Change and Firm Performance

According to Fama and Jensen (1983), board of directors is recognised as an invaluable mechanism to monitor management performance and to protect the interests of shareholders. Board change, on the other hand, refers to the appointment of a new member of the board in a year (Fox & Opong, 1999).

It is evident that the board of directors' actions are taken on behalf of the stakeholders in order to drive the company and to be the first line of defence to protect the stakeholders' interests against management decisions, if they are incompetent and ineffective. Board members have power and influence over aspects of the firm, including strategy, policy and decision making (Ghabayen, 2012). In this situation, board change is a significant event in a firm where the board appoints a new member on the board or a current member leaves his seat or for any other reason.

The board members' main target is to achieve the shareholder's objective and at the same time to achieve the target of the owners. So, the agency theory postulates that the board's aims are to monitor and improve performance (Fama & Jensen, 1983) while undergoing board change to bring in new blood to the board and to be active in order to achieve their aims. On the other hand, from the perspective of the resource dependence theory, the variety of board members provide multiple knowledge and experience which enhances performance (Pfeffer, 1972) and hence, this current study expects board change to improve firm performance.

In the context of Oman, the board of directors' role in CG is crucial. Theoretically, the responsibility of making sure that firms are managed properly lies in the hands of the shareholders. But, owing to the separation of ownership and control in almost all major business enterprises, it becomes the responsibility of the board of directors to ensure that top managers are performing their duties in an effective and efficient manner. The board is responsible for acting in the shareholders' and stakeholders' interests (Hampel, 2007).

A change in the board occurs for various reasons and among those; firms may appoint new members to the board in order to increase organisational effectiveness; second, firms may appoint new members to reveal specific strengths in certain areas; third, although not all new appointees agree, it may be argued that a new appointment is made only if it means improving efficiency (Fox & Opong, 1999).

Furthermore, the chief executive of popular global businesses related that the best companies view change as the most amiable method to win. In other words, companies view change as a journey while they understand the significance of guidance and experience, and more importantly, they are capable of learning from their successes and failures compared to their counterparts (Borstadt, 1985).

In a related study, Fox and Opong (1999) stated that board composition changes could be advantageous for various reasons. The directors can influence firm policies and objectives and in turn, its performance. Intrinsically, a new appointed member to the board may be able to bring fresh and innovative ideas to the firm operations. In addition, invaluable experience and knowledge can be brought in by appointing a qualified and experienced executive. Second, replacing an ineffective board member indicates that the firm is beginning to take steps to increase efficiency, which in turn will enhance future performance. Owing to the indiscernible contribution of individual members of the board, the performance of a firm's share price can be utilised as an indirect measure of the need to change the company board independence. The study regarding the relationship between board change and firm performance is quite new and hence, not a lot of studies exist on the topic.

Consistent with the above, Cahan and Wilkinson (1999) analysed the relationship between board independence and regulatory change in New Zealand. They used a regression model to test the association between independent variables and a dependent variable. This study selected 69 New Zealand companies listed on the New Zealand stock

exchange through the period 1992 to 1995. They found a significant association between board composition and regulatory change. This study recommended the indirect study of the interconnection between board change and firm performance to highlight the importance of the board change in improving firms over time.

To date, there is no study that has investigated the relationship between board change and firm performance in the developing countries including Oman. Hence, the present study contributes two elements; it provides firm performance effects of board changes (provides insight into the effects of board changes on firm performance) in Oman, and second, it is the pioneering study that tests the relationship between board change and firm performance.

The significance of board change lies in the introduction of new blood to the board of directors with guaranteed additions of experience, knowledge and new insight with higher motivation. This present study is going to fill this gap and considers testing this variable with firm performance.

In the context of Kuwait, Al-Matari *et al.* (2012) examined the relationship between board characteristics and firm performance in companies of Kuwaiti listed companies. They encouraged future researchers to study some variables such as the board change, the role of secretary on the board and the role of the executive committee on firm performance. From this recommendation, the current study is the first study to examine the association between board change, the role of secretary on the board and the role of

the executive committee with firm performance and expects that board change and the executive committee play vital role to improve the performance of companies.

3.5.5 The Role of the Secretary on the Board and Firm Performance

The role of secretary on the board is crucial in the board and is measured by using a dummy variable. The secretary primarily occupies a senior position in a private sector company or public sector organisation, equivalent to a management position or above (Zimmerman, 1997). The majority of American and Canadian publicly listed companies refer the company secretary as the corporate secretary or the secretary. The company secretary's responsibility includes the efficient administration of the company, in terms of guaranteeing company compliance with statutory and regulatory requirements and guaranteeing that the board of directors' decisions are being implemented (general theory). This study expects that the secretary role improves firm performance through the arrangement of board tasks.

Moreover, the company secretary is considered as the representative in the legal documents as it is the secretary's responsibility to make sure that the company along with the directors are running the company according to the law. The secretary is also responsible to register and communicate with the shareholders, to make sure that the dividends are paid and to keep company records updated – including the lists of directors, shareholders and yearly accounts (Murray, 1982). In most countries, private companies

are required by law to select a person to be the company secretary – a person who often occupies the position of a senior board member.

Regarding the agency theory, the separation of two positions in the company helps improving and safeguarding the rights of shareholders (Jensen & Meckling, 1976). Whereas, from the perspective of resource dependence theory, the separation of two positions in the company may not assist in the improvement of shareholder value (Pfeffer & Slanick, 1979). Hence, the current study suggests that the role of secretary on the board improves firm performance.

The secretary's primary role is to ensure that the firm is running the business in the right direction. The secretary secures official forms and correspondence, files the official documents in a timely manner and meets the formal requirements. If administrative staff is involved, the secretary is responsible to monitor his/her activities and the secretary also ensures the smooth running of the management committee (Creative Commons, DIY Committee Guide, UK). It goes without saying that the company secretary's selection should be carried out in a careful manner as he/she will handle the company's compliance welfare (Bates & Leclerc, 2009).

The value of this function either in private or in public companies is very important to arrange their meeting and coordinate between all departments in a firm to create and innovate to achieve the target of the firm. The role of the secretary is to keep all documents of the meeting and draw up a report of what every department must have to

achieve and for the next meeting, mention what each part managed to achieve or otherwise. Therefore, this function is important in monitoring and controlling every department related to the board. The role of the secretary is considered very active and it facilitates the high performance of the firm in the short term. In sum, this function helps the other committee to satisfy shareholders and interested parties related to firm in terms of wealth maximisation. As this function is only slightly mentioned in the Omani Code of Corporate Governance (2002) in Article (6), so its importance is not emphasised and therefore, no further information has been highlighted about it. Despite this fact, every firm listed on the MSM mentions the role of the secretary and some of them appoint one person to this position.

In general, this current study recommends that regulators develop the improved Code of Corporate Governance to match the global codes of corporate governance, which have a primary target of attracting significant numbers of investors from everywhere and ensure them to come and invest their money without concern for future crisis.

The role of secretary in the firm is very valuable; where he/she always writes meeting points and keeps record of the meeting and attendance of members every time. The secretary tries to follow the implementation of the board decision and make a report of what has been done. The secretary is the communication link between the board and other committees to achieve the meeting decisions. The role of secretary on the board includes arranging all the board's tasks, providing a clear picture about what they discussed and what they should do. The current study considers the importance of this

variable on the board structure. This is also, consistent with the recommendation of Al-Matari *et al.* (2012). Hence, it is important to study the role of the secretary on the board in firm performance.

3.5.6 The Legal Counsel and Firm Performance

At this point, although the importance of the legal counsel in a firm is evident to give assurance of investors and to solve problems of judicial allegations, which a firm may face during its operational period, yet the role of this job is not mentioned in the Omani Code of Corporate Governance (2002). Moreover, one term of poor performance displays by the Omani companies may be attributed to the lack of this basic function in the Omani Code of Corporate Governance. Therefore, the regulators must adopt this function and highlight its significance in the Code of Corporate Governance in Oman, if the country is desirous of attracting both local and foreign investments. The administrators must also add this function and highlight its significance to be at par with the Global Code of Corporate Governance. As understood, it is very critical to lose or win investors around the world because the world is like a small village. A company may conduct business from anywhere around the globe and this calls for the establishment of regulations and laws to keep businesses on track.

The legal profession, influencing board structure, is still largely undiscovered. Initiatives for investigation have been launched, but questions concerning what constitute board independence and its influence on the board structure are still unclear (Rose, 2006). The

present study employs legal counsel, whether or not the firm has legal counsel and measures legal counsel by a dummy variable.

Although several recommendations were brought forward concerning the board independence in the form of soft law in some European capital markets, but whether such recommendations are advantageous to the shareholders or not, are still ambiguous. An in-depth understanding of the definition of board independence may serve as a guideline for prosperous future work on the topic. According to Juras and Hinson (2008), further study may well explore legal profession on the board.

Moreover, firms may appoint external directors after a decline in performance to introduce new ideas and contribute to the knowledge pool or to inform the stakeholders that operations are under control (Pearce & Zahra, 1992). Similarly, Davis and Thompson (1994) claimed that the threat of lawsuits may also urge the appointment of external directors in order to control management. By itself, the present study is considering legal counsel as an additional variable.

The role of legal counsel in the firm is very essential to mitigate allegations of judicial matters. It expects to give a firm, clear insight into future contracts with investors and to solve any problem related to legal gaps. With regards to agency theory, the separation of jobs provides authority to make the right decision, to directly monitor firms and to evaluate and provide a report on its weaknesses. It also tries to improve the highlighted weak points (Al Busaidi, 2008).

In the context of the resource dependence theory, the outsource will give a firm lots of experience and knowledge to deal with the transaction during the life cycle (Rao, Al-Yahyaee & Syed, 2007). Then, the legal counsel motivates firms to stay on the right track all the time without any problems with all the interested members. With regards to the Omani Code of Corporate Governance, the firm should have legal counsel to revise any deeds related to legal matters for example, formulation of contracts, revision of legal code inside firms, organising the relationship between the firm and investors, solving any problem faced by the firm at any time whether local or foreign. It tries to plead for the company in light of the company's rights to third parties and others.

Despite the importance of legal counsel in the current time and its relation to CG, prior studies have largely ignored its existence. The current study is the first study to consider the importance of legal counsel with firms' performance as advised by Al-Matari *et al.* (2012), who recommended studying the relationship of legal counsel with firm performance. Given the importance of this factor in helping companies to improve their performance, the main target of this study is to investigate the association between legal counsel and firm performance.

3.5.7 Foreign Member on the Board and Firm Performance

In this section, this study provides important variables that will help academically and practically, and assist policymakers to understand how to improve the Code of Corporate Governance in practical life. This study manages to cover a wide variety of CG in which

to realise improvement in firm performance. In addition, the board of directors is among the many internal governance mechanisms that cater the alignment between shareholders and managers' interests and disciplining of management teams (Barnhart, Marr & Rosenstein, 1994; Park & Shin, 2003). Moreover, foreign member on the board stands as among the significant governance issues that are presently confronted by contemporary organisations.

The key issue of board diversity is very useful to enhance the board performances and to make the right decision. This variable is measured by the ratio of foreigners serving on the board to the total numbers. Foreign directors bring with them invaluable knowledge concerning contextual issues in foreign markets and hence they contribute to the strategic decision making quality (Zahra & Filatotchev, 2004). They are also less likely to be associated with firms and its management and are therefore independent (Van & Ingley, 2003).

Hence, from an agency theory perspective diversity of nationalities on the board may improve monitoring, thus resulting in better firm performance. In the same context, Oxelheim and Randoy (2003) found that foreign board members have significant positive impact on firm performance. They argued that having a foreign member on the board signals a greater commitment to monitor management, transparency and thus enhance the reputation in the financial market, which leads to a superior firm value. It is argued that foreign directors in family firms can bring valuable knowledge and expertise. They can make the board more efficient in terms of monitoring.

Furthermore, foreign directors may bring much needed expertise and diversity, especially for companies that operate globally. In addition, for countries with relatively weak legal and governance institutions, importing directors may be an approach to improve governance at the firm level and reduce the firm's cost of capital by signalling its willingness to bond to the possibly higher governance standards of the foreign directors' home country (Miletkov, Poulsen & Wintoki, 2011). On the contrary, foreign directors are inherently costly. They may come from a different culture, speak a different language, be physically distant from the companies on whose boards they serve, and may demand a higher level of compensation for the inconvenience of serving on boards outside their own country of residence. From another perspective, the resource dependence theory stresses on the importance of foreign directors inside firms as they give a lot of foreign experience and foreign knowledge to help firms to solve any problem inside multinational firms and to help employees in dealing with foreign problems if any arises (Pfeffer & Salancik, 1979).

On the other hand, foreign directors give international investors assurance and confidence. Consequently, there are few studies in the developed countries that have directly explored the relationship between foreign directors and firm performance. However, there is a lack of investigation of this variable in the emerging market. Therefore, the current study considers adding it to the group of board diversity as a moderator between board structure and firm performance. The findings are still mixed between the two. Miletkov *et al.* (2011) found a negative relationship between foreign

directors and firm performance while Ruigrok, Peck and Tacheva (2007) found no association between them. Nonetheless, very little number of studies has been done to test this relation as explained below.

Miletkov *et al.* (2011) examined the association between foreign directors and firm performance in 98 countries. The sample comprised of 20,000 companies and data was selected in 2005. This study used Ordinary Least Squares (OLS) regression to analyse the interrelationship between foreign directors and firm performance. The finding reveal a negative relationship between foreign directors and firm performance. Contrastingly, Ruigrok *et al.* (2007) studied the impact of nationality (foreign) and gender on the corporate board in Switzerland. This study used few control variables for example – directors' age and directors' tenure. The sample selection comprised of 210 publicly listed firms in Switzerland for the period of 2003. It used probit regression analysis to examine the association between board diversity and board directors. The findings discovered that there is an association between nationality (foreign), gender and the corporate board.

The above discussion highlights that the foreign members improve performance of the company. Although the importance of this variable is clear, up till now very little study (to the knowledge of the researcher) has been conducted to examine this relationship.

3.6 Audit Committee Characteristics and Firm Performance

It is important to note that audit committee size, audit committee independence and audit committee meeting, presumably, could continue to serve as the corporate regulators to ensure the management accountability and responsibility towards shareholders by ensuring that managers present true and fair view of the firms and avoid irregularities. Therefore, size, independence and meeting of the audit committee characteristics will serve as a good blend of CG structure in creating firm's performance. Previous studies revealed mixed findings concerning the relationship between committee characteristics and firm performance as explained in the next sub-section.

3.6.1 Audit Committee Size and Firm Performance

The size of the audit committee is considered as the first factor of audit committee characteristics. It is measured by the number of members serving on the audit committee of the firm (Bauer *et al.*, 2009; Hsu & Petchsakulwong 2010; Nuryanah & Islam, 2011; Obiyo & Lenee, 2011).

The audit committee is primarily developed to help the BODs oversight function in an attempt to increase financial disclosure. In the midst of increasing numbers of financial reporting scandals, the audit committee's role in CG has been currently the topic of discussion among policymakers, managers, investors and academics. The main function of an audit committee is to hold regular meetings with the external and internal auditors to go through the financial statements, to assess risk and audit the firm's internal controls.

This assists in alleviating agency issues with a timely publication of authentic accounting information from the manager to shareholders and other groups who depend on the information. This minimises the information asymmetry between insiders and outsiders (Heenetigala & Armstrong, 2011).

In the 20th century, following the biggest American corporate scandal of Enron and WorldCom, the Sarbanes-Oxley Act (2002) has become the magna carta of corporate disclosure and internal control, especially in relation to issuance of the duties of an audit committee. Recommendations are suggested by the Blue Ribbon Committee (BRC) to improve the effectiveness of a corporate audit committee (BRC, 1999). It recommends three important points that should be strengthened: independence, effectiveness and accountability. Moreover, the Cadbury Commission recommends that audit committees should be established. It also recommends that audit committees should have a minimum size of three members and should consist of solely Non-Executive Directors (NEDs). In the same context, the Omani Code of Corporate Governance (2002) mandates that the committee should be comprised of at least three members who are all non-executive directors and majority of them have to be independent. The committee chairman should also be independent and at least one member is an expert in finance and accounting.

In Asia, following the Asian crisis, the effectiveness of the audit committee was being questioned. Thus, there is a great concern about the effectiveness of audit committees (Allen, 2000). In fact, the phenomena of corporate collapse around the world have led to legislation or regulation reforms in both the accounting field and the stock exchange

(Allen, 2000; Australia 2002; Clarke, 1998). The audit committee can play a key role in monitoring and improving the quality of information between firm owners and managers (Abdurrouf, 2011).

In a related study, Bozec (2005) and Garcí'a-Meca and Sa'nchez-Ballesta (2011) examined the relationship between CG and firm performance in Canada and Spain respectively. They recommended that future research should study audit committee factors with the board of directors due to its importance. From their recommendations, the current study examines the audit committee with other dimensions of CG.

The audit committee is one of the main elements of the CG system that plays a key role in monitoring the internal control framework effectiveness. It oversees and reviews the process of financial reporting of a firm as well as acts as an intermediary among internal auditors, external auditors, managers and board of directors to establish the proper flow of information among them and to guarantee transparent reporting (Fama & Jensen, 1983; Jensen & Meckling, 1976). Moreover, one of the key roles of an audit committee is to ensure the quality of financial reporting and control systems. The audit committee is one component of the set of monitoring mechanisms available for reducing information asymmetry between insiders and outsiders (Kim & Yoon, 2007). The audit committee is the most dependable mechanism that protects the public interests (Abdurrouf, 2011; Kyereboah-Coleman, 2007).

Moreover, audit committee bridges the communication network between internal auditors and external auditors. It helps the board of directors in their activities, such as nominating auditors, revising the audit scope, the audit results, internal financial information and publication of financial reports (Chanawongs, Poonpol & Poonpool, 2010). In the same context, the presence of audit committee plays an important monitoring and controlling role of management activities, which results in increased performance of the firm (Rahmat *et al.*, 2009; Xu *et al.*, 2005). In the same way, audit committee can reinforce the board in its implementation, monitoring and maintaining good CG practices that benefit the firm and stakeholders (Saibaba & Ansari, 2011).

With reference to the Omani Code of Corporate Governance (2002), the roles of the audit committee are listed as follows;

1. Selection of the name of the auditor according to independence (specifically when offering other non-audit services), fee and terms of service and forwarding the name to the board to present before the AGM for appointment.
2. Revising the audit plan and the findings of the audit to clarify whether the auditors are privy to all the needed documents.
3. Reviewing the financial statement for financial fraud, specifically any fraudulent and fictitious parts of the statement. A suitable system should be established to make sure that appropriate accounting policies and principles of fairness are in place in the financial system.

4. Monitoring the internal audit function on its entirety with particular focus on reviewing the internal audit plan scope of the year, reviewing the reports of internal auditors relating to critical areas, reviewing the internal auditing efficacy and ensuring that internal auditors are privy to all the needed documents.
5. Monitoring the sufficiency of the internal control system through the external and internal auditors' regular reports. Appointing an external consultant if needed.
6. Monitoring the financial statements, particularly the reviewing of annual and quarterly financial statements prior to their issuance, review of the draft financial statements qualifications and discussion of the accounting standards and principles. Discussion of any changes in accounting policies, principles and accounting estimates compared to the prior year, any employment of novel accounting policy, a critical review of any deviation from the International Accounting Standards (IAS) and non-adherence to the disclosure mandates laid down by CMA.
7. Playing the role of a channel of communication between external auditors, internal auditors and the board.
8. Reviewing the proposed transactions with relevant parties for providing recommendations to the board and establishing rules for contracting with parties in small value transactions prior to taking the audit committee and the board's approval.

These listed regulations and the CG code serve as yardsticks that guide the Omani limited listed companies and their operations. The level of adherence clearly reflects well-governed firms from their counterparts.

In the present section, the present study discusses suggestions provided by prior authors including, Forker (1992) who claimed that the audit committee's existence may lead to the enhancement of internal control and in turn serves as a monitoring mechanism to improve firm value (Kim & Yoon, 2007). In addition, a larger audit committee is proposed to serve as a stricter monitor, but makes it challenging for conclusions to be reached (Hsu & Petchsakulwong, 2010). In general, the quality of the audit committee is primarily related to the quality of the corporate board from which the committee stems from; both policy makers and academics have also stated that board structure determines the quality of financial statement (Pagano, Schwartz, Wagner & Marinelli 2002; Vafeas, 2005).

Overall, the principles of CG indicate that audit committees should be independent in their work and they should take care to employ professional care. In instances of any financial manipulation, the audit committee is accountable for their decisions and actions as the existence of transparent financial information minimises the information asymmetry and enhances the firm value (Abdurrouf, 2011; Bhagat & Jefferis, 2002).

After the importance of the audit committee is globally verified and following the explanation of the role of an audit committee in light of the Omani Code of Corporate

Governance (2002), it can be finally stated that the audit committee helps a firm to improve its performance and it can attract the confidence of investors whether local or foreign. The financial report is very essential and sensitive matter for anyone looking for investing in a new environment. Therefore, the audit committee has to approve satisfaction of the annual report. The current study offers an extensive discussion of the terms of several theories, namely, agency theory and resource dependence theory.

Regarding agency theory, the manager-shareholder conflict is what encourages management to make decisions in their best interests and not in the shareholders' interests particularly when management is very opportunistic (Jensen & Meckling, 1976). The lack of independent and effective control procedures tempts the company management to deviate from safeguarding the interest of shareholders (Fama & Jensen, 1983). Therefore, effective and efficient audit committees are required to resolve the said conflict (Klein, 1998) and to keep up the good performance (Charan, 1998; Rahmat *et al.*, 2009). According to Dalton, Daily, Johnson and Ellstrand (1999), audit committees become ineffective if they are either extremely large or extremely small. Specifically, a large audit committee tends to lose concentration and participation compared to a small one.

Arguing in favour of the agency theory and its proponents, when the number of members is bigger, the firm will display poor performance. Authors from around the world examined the relationship between audit committee size and firm performance, whether in developed countries (Bozec, 2005) or in the developing countries (Al-Matari *et al.*,

2012b; Hsu & Petchsakulwong, 2010; Mollah & Talukdar, 2007). In the end, they found a negative association between them. For more details, refer to Table 3.10 in Appendix A.

On the other hand, the resource dependence theory states that when the board of the committee is bigger, a better performance is achieved. A small audit committee lacks the diversity offered by a large one in terms of skills and knowledge and this makes the committee ineffective. An audit committee with just the right number of members enables members to utilise their experience and expertise for the benefit of the stakeholders (Pfeffer, 1987; Pearce & Zahra, 1992).

Supporting the resource dependence theory, there are many researchers who found a positive relationship between audit committee size and firm performance in developed countries including Bauer *et al.* (2009), Khanchel (2007), Premuroso and Bhattacharya (2007) and Reddy *et al.* (2010). On the other hand, in the developing country, studies by Al-Matari *et al.* (2012), Black and Kim (2007), Black, Jang and Kim (2003), Danoshana and Ravivathani (2014), Heenetigala and Armstrong (2011), Kyereboah-Coleman (2007), Obiyo and Lenee (2011) and Swamy (2011) found a positive association between these two. For more information, refer to Table 3.10 in Appendix A.

From a general perspective, from the agency theory and the resource dependence theory, mixed findings are found. Some studies found no relationship (insignificant) between the audit committee and firm performance; for example in the developed countries, the study

conducted by Wei (2007) and in the developing countries by Abdurrouf (2011), Ghabayen (2012), Kajola (2008), Kim and Yoon (2007), Kyereboah-Coleman (2007), Noor (2011), Rahmat *et al.* (2009), Nuryanah and Islam (2011) and Rahmat *et al.* (2009). For more information, refer to Table 3.11 in Appendix A.

3.6.2 Audit Committee Independence and Firm Performance

The second key of quality of the audit committee characteristics is its independence. Generally, the audit committee should have at least three directors with 2/3 of the member's non-executive directors. The chairman is chosen from among the 2/3 members and must be appointed by the board. The audit committee independence is measured through the ratio of non-executive members on the committee (Abdullah *et al.*, 2008; Kang & Kim, 2011).

The non-executive members of the committee play a key role in guaranteeing that CG practices of auditing are adhered to effect financial report (Swamy, 2011). This is supported by Abdullah *et al.* (2008) who stated that firms with majority of inside directors and lacking an audit committee are more inclined to commit financial fraud compared to a controlled sample with a matching industry and size. Consequently, audit committees characterised by higher members of non-executive directors are observed to be more independent compared to those characterised by more executive directors (Rahmat *et al.*, 2009).

Consequently, the Sarbanes-Oxley Act (2002) made it compulsory for audit committees of listed companies to comprise of independent directors and the current modifications to the Oman CG framework which was introduced in 2002, mandates that the committee should consist of at least three members who are non-executive with majority of them independent. The committee chairman should also be an independent director (Omani Code of Corporate Governance, 2002). For more information about the Omani Code of Corporate Governance (2002), refer to Appendix B.

From both the agency theory and resource dependence theory, the autonomy should be given to make the right decision without any restriction or condition, and to work in detecting errors and revealing them without any problems because the independent reviewers are not related to the company in any way. In addition, the relationship between audit committee independence is expected to be positive but there are only few studies that examined the relationship between audit committee independence and firm performance both in developed countries (Dey, 2008; Khanchel, 2007) and developing countries (Abdullah *et al.*, 2008; Chechet, Jnr & Akanet, 2013; Nuryanah & Islam, 2011; Saibaba & Ansari, 2011; Swamy, 2011; Yasser *et al.*, 2011). They found a positive association between the audit committee independence and firm performance. For more details, refer to Table 3.12 in Appendix A.

On the other hand, some researchers found a negative association between audit committee independence and firm performance in both developed countries and

developing countries (Dar *et al.*, 2011). For more information, refer to Table 3.13 in Appendix A.

In the end, there are some researchers who found adverse results in prior outcome and revealed no relationship (insignificant) between audit committee independence and firm performance, including Al-Matari *et al.* (2012a), Al-Matari *et al.* (2012b), Dar *et al.* (2011), Ghabayen (2012), Khan and Javid (2011), Kota and Tomar (2010), Kyereboah-Coleman (2007), Noor (2011) and Rahmat *et al.* (2009). For more details, refer to Table 3.14 in Appendix A.

3.6.3 Audit Committee Meeting and Firm Performance

The audit committee meeting is the third vital factor of audit committee characteristics. Previous literature utilises the meeting frequency to measure the activeness of the audit committee (Hsu & Petchsakulwong, 2010; Khanchel, 2007; Kyereboah-Coleman, 2007; Rahmat *et al.*, 2009).

The audit committee's effectiveness in conducting its overseeing role of financial reporting process and internal control calls for regular meetings (Vafeas, 2000). In addition, the meetings have to be conducted at least three or four times a year and the chairman must control and structure them (Hughes, 1999; McMullen; Raghunandan, 1996).

In the same context, frequent and controlled meetings would be invaluable in helping audit committees examine accounting and internal control system, and informing top management concerning the committee's actions (McMullen & Raghunandan, 1996). An executive director would explain the procedures and issues that may have cropped up (Hughes, 1999). Prior evidence is consistent with the guidelines provided by the Cadbury Committee (1992) in the UK and the BRC (1999) in the US. The guidelines mandate audit committees to hold meetings not less than three times yearly. This is consistent with the Omani Code of Corporate Governance (2002) that mandates the committees holding of meetings at least four times yearly with a majority of independent directors. A properly planned meeting schedule guarantees the timeliness of the decision of the committee and the audit cycle and the financial statements issuance.

Additionally, an audit committee that has frequent meetings is more proficient in the effective monitoring role of financial activities such as the preparation and reporting of the company's financial information (Rahmat *et al.*, 2009). Similarly, the audit committee has to maintain a certain degree of activity in order to carry out its function through the frequency of meetings (Be'dard *et al.*, 2004; Khanchel, 2007) particularly to avoid the enforcement actions of the Securities and Exchange Commission (Abbott *et al.*, 2004; McMullen and Raghunandan, 1996).

Consistent with the suggestions of previous studies, the evidence provided by Hsu and Petchsakulwong (2010), Kalbers and Fogarty (1993) and Menon and Williams (1994) stated that audit committee diligence is related to its effectiveness. Moreover, they

claimed that frequency of meetings reflects diligence. Additional to that, Abbott, Peters and Raghunandan (2003) also stated that frequent meetings of the audit committee may lead to enhanced financial accounting processes and in turn, superior performance.

Consistent with some discussion above, the audit committee meeting is invaluable in improving firm performance as mentioned. Sharing a similar direction from the resource dependence theory, the board meeting helps the board to evaluate and pursue the board business from time to time and to solve any problem faced by employees (Pfeffer, 1987; Pearce & Zahra, 1992). Hence, when the frequency of board meeting increases, the performance of the firm is also increased. If the committee holds more meetings during a year, the company will be mindful of its endeavour to achieve its target because more meetings help firms to figure out any problem and find solutions in a timely manner and to enhance the relationship between members and conduct a close negotiation when needed.

Regarding the above discussion and in support of the resource dependence theory, the audit committee meeting has a positive relationship with firm performance. However, little research has been done on this association and they found a positive relationship between the audit committee meeting and firm performance both in the developed countries, for example Khanchel (2007) and in developing countries by Chechet, Jnr and Akanet (2013), Kang and Kim (2011), Kyereboah-Coleman (2007) and Saibaba and Ansari (2013). For more details, refer to Table 3.15 in Appendix A.

From the other perspective of the agency theory, Jensen (1993) revealed that boards should be inactive and its activity reflects a reaction to adverse performance. Jackling and Johl (2009) and Lipton and Lorsch (1992) also believed that the more frequent the meetings are, the more likely they will lead to superior performance of the firm. More specifically, frequent meetings every year indicate that the board is playing an operational role as opposed to an oversight role and it is generally believed that the role of the board is to govern management not to manage the firm.

Moreover, Rebeiz and Salame (2006) stated that meeting quality matters most and the frequency does not always improve firm performance. A survey by Klynveld Peat Marwick Goerdeler (KPMG30) revealed that audit committees perceive that their effectiveness may be hindered or adversely affected by full agenda and compliance activities. Nevertheless, so few studies have been carried out to investigate the relationship between audit committee meeting and firm performance, whether in the developed countries or developing countries as it has been explained and discussed in this section.

In the context of Thailand, Hsu and Petchsakulwong (2010) examined the relationship between audit committee meeting and performance efficiency of public Thai non-life insurance companies for the period from 2000 to 2007. The insurance efficiency performance was utilised to calculate data envelopment such as technical, allocative, cost and revenue efficiency. This study used truncated bootstrapped regression and found a

negative impact between audit committee meeting and performance efficiency. Please refer, to get more information regarding this relation to Table 3.16 in Appendix A.

From a general perspective, no insignificant association had been found between audit committee meeting and firm performance as evidenced by Al-Matari *et al.* (2012a), Al-Matari *et al.* (2012b), Kyereboah-Coleman (2007), Noor (2011) and Rahmat *et al.* (2009). More details can be obtained from Table 3.17 in Appendix A.

3.7 The Executive Committee and Firm Performance

The executive committee is a sub-committee of the board such as purchase committee and remuneration committee. The executive committee unfortunately like other committees, is not considered at par with the audit committee in the Code of Corporate Governance (2002). Although executive committee is an essential element of board structure, but there is no study (to the knowledge of the researcher) that has investigated its relation with firm performance. Hence, the present study provides insights into the importance of the executive committee.

The executive committee exercises the powers and functions vested in it by the board of directors with respect to certain specific issues relevant to the institution, its bidding policies and other urgent matters referred to them by the management of the institution and in accordance with the provisions of the list of the powers, authorities and the procurement system and acquisition of assets accredited institution. The executive committee has been configured to facilitate decision-making when there are difficulties

for the meeting of the governing council of the whole. Executive committee focuses on strategic issues and is responsible for all matters related to the budget and procurement. The committee has the powers and the appropriate authorities to guide and direct management to ensure that the company's operations are managed readily and conveniently.

With the global financial crisis of recent times, which led to the collapse of many of the global commercial entities a big lesson has been learned by business entities and they have employed appropriate strategies for executive management. Therefore, executive management has become one of the most important elements in the context of generating revenue and maximising shareholder value while maintaining the economic stability of the country in which they operate (Al Rashid & Jamal, 2010).

The executive management concept has become increasingly significant to corporate governance. Aligned with the risk-based method, a board establishes a firm-wide risk management system that heightens risk awareness in the firm. The increase in awareness and knowledge enables the board to take efficient and effective decisions to create a positive effect on the governance structures and on the firm's control environment. In addition an effective CG is constantly evolving based on command-and-control dictums to reach a more dynamic process, identifying, and managing risk throughout the organisation (Al-Rimawi, 2001).

The board of directors possesses executive management responsibilities described by best practices, guidelines, laws and regulations. The executive committee is responsible for assisting the BOD in studying the various types of executives to which the organisations are vulnerable to. These responsibilities also include the execution of the organisation's executive management policy.

Additionally, the executive committee should also perform oversight responsibilities and provide evidence for the effect. The committee members must be directly linked to management and be the recipient of direct reports from management. The committee must also be comprised of at least three members with a majority of non-executive director. At least one member should be a member of the audit committee, and one must be a risk expert. Moreover, the committee chairman should be a non-executive director (Omani Code of Corporate Governance, 2002).

The board members should be familiar with the new environment and responsibilities to protect their reputation and the organisational wealth. They should have to be privy to the risks in order to perform their duties based on the highest principles and best practices.

Generally, the main tasks of the executive committee are briefly provided as overseeing the company's business on behalf of the board of directors and overseeing the implementation of the internal regulations governing the work of the company, such as a list of tenders and a list of purchases, strategic investment decisions, cash management and liquidity, business plans and budgets, significant changes in the policies and

procedures, suggestions for any new business, review developments in performance, matters relating to the staff of the company and any other matters the board of directors forward to the committee. As mentioned in the annual report of the companies, the tasks of the executive committee are as follows (2008 to 2012):

1. To review the vision and business strategy of the company and its business plan.
2. To conduct a periodic review of the company's financial and operational performance and to scrutinise the management proposals concerning write-off and list recommendations for the council.
3. To review the annual budget of the company and pass recommendations around the board for approval and accreditation.
4. To oversee the transformational processes of the company, including mergers and acquisitions.
5. To review the company's risk management and follow-up legal issues.
6. To prepare policies concerning staff remuneration, wage payment, incentives, recruitment, administration, senior management evaluation and compensation system revision and to prepare bank executives.
7. To review the management proposals of the company with regards to bad debts and submit recommendations to the board of directors.
8. To adopt the participation of the company and public tenders according to the approved board powers.

9. To review the company's marketing plan and recommend the adoption of the governing council.
10. To represent the board of directors of the external parties.
11. To go through the suggestions and studies which are related to investments and make recommendations to the board of directors concerning investment opportunities, diversification and development plans.
12. To take appropriate actions on the issues highlighted by the board of directors or by the president of the board of directors.
13. To take appropriate actions on important matters highlighted by the chief executive officer of the company this comes under the commission's jurisdiction.
14. To approve expenditures within the boundaries set by the board of directors.
15. To review and approve recommendations in terms of awarding tenders and procurement and contract values those are within the boundaries set by the board of directors.
16. To conduct audits on the services/products quality and effectiveness offered by the company and to recommend optimum methods for development and improvement.
17. To guide management on the issues of strategic priorities and risks those are related to the operations and strategic financial investments.
18. To hire independent consultants to help in achieving firm goals.
19. To approve the bank facilities renewal and general expenses.

In addition to the above, the global code, Gulf code and Omani Code of Corporate Governance (2002) failed to highlight the significance of this committee, although it has an important role to assure investors to invest without concern about risk in the future and provide the board with a report concerning risk in any operations whether in current situation or in the future. It is also important to note that the Omani Code of Corporate Governance established in 2002 has not been updated according to the development taking place in the global code. Therefore, the capital market authority must update Omani Code of Corporate Governance in order to keep pace with the evolution in the world to encourage both local and foreign investors to come and invest in the country. Regarding the importance of this committee, this current study aims to test the relationship between the executive committee and firm performance.

There are several previous studies that have examined the association between the executive committee and other variables, but no studies have tested its relation to firm performance.

Al-Matari *et al.* (2012) also investigated the association between board characteristics and firm performance among Kuwaiti firms. They recommended further studies to consider the relationship between the executive committee and firm performance. As a matter of fact, the investigation of the effect of the executive committee on the firm performance is still lacking and has been greatly neglected in the literature. Based on these reasons, the current study focuses on taking this variable into account and bridging

the gap in the literature because executive committee helps companies to reduce and avoid future risks.

3.8 Underpinning Theories

This section highlights the theories utilised in the present study. Although there are several theories related to CG such as agency theory, resource dependence theory, stewardship theory, institutional theory, stakeholder theory, transaction cost theory, political theory, ethical theories, tournament theory and others, but this study has taken popular ones like agency theory and resource dependency theory which have become prominent over the recent times. With regards to the recommendation by Al-Matari *et al.* (2012), they recommend testing some theory with firm performance, such as stakeholder theory, stewardship, resource dependence theory and others. This present study considers the agency theory and resource dependence theory as they have related variables to this study.

3.8.1 Agency Theory

Agency theory is generated from the study conducted by Berle and Means (1932) concerning the separation between ownership and control in large firms. The most widely-cited studies of agency theory come from Jensen and Meckling (1976). It is a theory based on the relationship between the principal who is the owner and the agent who is the manager. In contemporary corporations, the separation between ownership and management offers the context for the agency theory function.

This is the case because contemporary organisations are characterised by widely dispersed ownership in terms of shareholders who do not get involved in the companies' management. Intrinsicly, an agent is appointed to be the manager of the day-to-day firm operations. The separation between ownership and control leads to the possibility of conflicts of interests between the principals and the agents, which in turn, lead to high costs related to resolution of such conflicts (Eisenhardt, 1989; Jensen & Meckling, 1976).

According to Jensen and Meckling (1976), shareholders can be described as the residual claimants after other parties and hence, they have the weakest rights. Therefore, CG is mainly developed to safeguard and promote the shareholders' rights. Along the same line, they recommended that firms is considered as a link or connections, understood and explicit, among the many parties or stakeholders including bondholders, shareholders, employees and even the society.

Moreover, the interests of stakeholders are not always aligned and therefore, agency problems arise when the agent's interests are different from those of the principal. Depending on the parties involved in conflicts, the agency problems can be divided into managerial agency or managerialism which takes place between stockholders and management; debt agency which takes place between stockholders and bondholders; social agency which takes place between private and public sectors and political agency which takes place between public sector agents and the rest of the society/taxpayers.

In order to effectively limit agency costs caused by the separation of ownership and control, Fama and Jensen (1983) proposed that firms need systems which can distinguish between decision management and decision control. This would limit agency costs by controlling the power of management and ensuring the proper consideration of shareholders' interests. So, corporate governance may be seen as such a system.

Moreover, researches by Fama (1980), Fama and Jensen (1983), Shleifer and Vishny (1986) and Williamson (1984) claimed that opportunistic behaviour of management is minimised by CG mechanisms and internal and external CG mechanisms can decrease agency costs. McKnight and Weir (2009) also supported the latter contention.

In addition, the agency theory can be the basis of governance of firms throughout their various internal and external mechanisms (Roberts *et al.*, 2005; Weir *et al.*, 2002) as governance mechanisms are developed in order to ensure agent-principal interest alignment, protect shareholder interests and thus to minimise agency costs (Davis, Schoorman & Donaldson, 1997).

This is consistent with Demsetz and Lehn (1985) who stated that the main purpose behind CG is not to improve corporate performance directly, but to tackle agency problems by overseeing the behaviour of management and examining the financial reporting process. Therefore, CG mechanisms are able to mitigate agency costs, protect shareholders' interests by monitoring management activities, and thus, keep the management interests aligned with the shareholders'.

The most important notion behind the agency theory is that managers are often incited by their personal benefits and they work to satisfy their interests as opposed to keeping the shareholders' interests into consideration and maximise shareholder value. For instance, managers may be more interested in owning luxurious offices, company cars and other items of their interest whereas the cost is paid by the owners.

Fama (1980) also stated that governance mechanisms are less costly to use when it comes to control management as compared to other alternatives like takeovers. Similarly, studies dedicated to management ownership focus on methods in which managers' compensation enables the alignment of their interests and that of shareholders (Bushee, 1998; Pound, 1988).

The audit committee is used as a decision control system for internal monitoring by the board of directors (Fama, 1980; Fama & Jensen, 1983). Requirements for monitoring suggest the need for external audits (Anderson *et al.*, 2004), audit committees (Bradbury, 2006) and the use of Non-Executive Directors (NEDs) (Anderson *et al.*, 2004; Fama, 1980).

Finally, CG using the executive committee, audit committee, board of directors and secretary role allow shareholders to monitor management actions accurately. Weak management monitoring may incite managers to satisfy their own interests like management earnings while, effective corporate monitoring with the help of good corporate governance can minimise management's adverse behaviour.

Based on the above discussion, the agency theory covers many variables related to this study such as board of directors' characteristics (size, independence, meeting, the role of the secretary and the foreign member on the board), the audit committee characteristics and the executive committee.

3.8.2 The Resource Dependence Theory

Another important theory, exploring corporate governance, especially the role that directors play in terms of the system of corporate governance, is the Resource Dependence Theory. The role of directors in the contemporary CG in the resource dependence theory complements the formerly discussed agency theory.

The resource dependence theory postulates that boards are selected to increase the supply of crucial firm resources (Hillman & Dalziel, 2003; Klein, 1998; Pfeffer & Salancik, 1979; Pfeffer, 1972). It also postulates that non-executive directors are the providers of connection with the external environment through their expertise, prestige and contacts. Moreover, according to Spencer (1983) non-executive directors, mostly view themselves as an advisor rather a decision maker and thus, they become influential and people pay attention to them although they are not policy instituting entities (Haniffa & Hudaib, 2006).

In addition, the theory considers the board of directors as those who span the boundary and gather resources from the environment (Pfeffer, 1972). Therefore, boards as effective linkage become an invaluable mechanism for firms to gain external resources.

Additionally, the resource dependence theory argues that the directors are valuable resources of the firm or the resource dependence role and they may fulfil the monitoring and resource dependence roles simultaneously (Hillman *et al.*, 2000).

Also, the resource dependence theory stated that the business environment is ripe with various external factors that may lead to uncertainty and external dependencies (Daily, Johnson & Dalton, 1999). Along a similar line, firms have to face those uncertainties-producing factors in order to succeed in the dynamic and competitive environment, directors are the link between the firm and the factors, and they assist firms in making superior investment decisions.

Moreover, to help in handling external uncertainties-generating factors, directors also possess crucial information, expertise, skills, and connections to relevant external stakeholders (customers, governmental agencies, creditors, and suppliers) which are important to the firms. Specifically, Williamson (1984) noted that external directors with significant experience in dealing with regulators and regulations may help in minimising transaction costs between the firm and the regulators and may enhance the board's operational efficiency.

The resource dependence theory offers a theoretical basis for the board of directors' role as a firm resource (Johnson *et al.*, 1996; Hillman *et al.*, 2000), while the appointment of the external board of directors assists in obtaining access to resources, which are important for the success of the firm (Johnson *et al.*, 1996). With regards to the role of

resource dependence, external directors provide resources to the firm, including information, skills and connection to crucial constituents such as suppliers, buyers, social groups, public policy decision makers, and legitimacy (Hillman *et al.*, 2000).

In addition, appointments of such directors reflect the value placed on capital because resource plays a key role in the individual firm behaviour. According to Stearns and Mizruchi (1993), a relationship between firms, borrowing strategy and the type of board financial representation is related and this association offers the parties with the chance to co-opt continuously.

In a pioneering study, Pfeffer (1972) revealed that the size of the board along with background of external directors is crucial to the management of organisational requirements for capital and regulatory environment. Moreover, the board also works as a boundary spanner in an attempt to improve the firm's business prospects.

The above finding is consistent with Hermalin and Weishbach's (1991) findings, which revealed that internal directors may be replaced by experienced external ones when the firm is performing poorly. Similarly, Pearce and Zahra (1992) showed that external directors are often appointed to introduce a fresh perspective during the firm's poor performing years. On the other hand, Donaldson and Muth (1998) stressed on the significance of the connections on which the resource dependence theory is associated with the improvement of the performance of the firm. In other words, the resource dependence theory considers the board as a resource that satisfies its resource

requirement, facilitates positive environment, and thus enhances the performance of the firm.

Based on the above debate, the resource dependence theory focuses on the sources supporting the firm in an attempt to achieve its aims whether out-resource or in-resource. Subsequently, these sources provide firms with experienced people either local or international, knowledge, diversity of people and certified educations for achieving the firm's aim, which in turn maximise shareholders' wealth. In sum, this theory covers the board of directors' characteristics, audit committee characteristics, the executive committee, board diversity such as, the number of foreign members on the board or committee. These factors have not been discussed in the agency theory in relation to firm performance. As such, the resource dependence theory is essential to cover these variables. In conclusion, the integration between the two theories namely; agency theory and resource dependence theory offers a clear insight into the association between CG determinants and firm performance.

3.9 Summary of the Chapter

This chapter covers many points, i.e. the corporate governance identifications, the importance of corporate governance, the performance identifications, and the importance of performance. Moreover, it presents the relationship between corporate governance dimensions and firm performance. Lastly, it provides the underpinning theories related to this study. The next chapter offers the research framework and hypotheses development.

CHAPTER FOUR

RESEARCH FRAMEWORK AND HYPOTHESES DEVELOPMENT

4.1 Introduction

The present chapter explains the theoretical framework as well as the formulation of hypothesis based on the relevant theories and empirical evidence as explained in the literature review chapter.

4.2 Theoretical Framework

This study utilises the agency theory along with the resource dependence theory in an attempt to examine the CG and FP relationship. On the basis of agency theory, the main problem explained by the agency appears under conditions of incomplete and asymmetric information. Another indication is the issue of key factors in most of the relations of employers and employees. For instance, when shareholders recruit senior executives from companies, they use different mechanisms to try to reconcile the interests of the agent with the principal's interests.

According to the agency theory, the delegation of the administrative responsibilities should go hand-in-hand with the mechanisms to supervise management performance and guarantee that the authority delegation leads to the highest possible returns. Consistent with this contention is the finding by Kyereboah-Coleman and Biekpe (2006), who found

that the agency theory lays down the relationship between board characteristics and the performance of the firm.

Agency theory expounds on the relationship between the owner and manager, and contributes to the separation of functions and works to strengthen trust between owners and managers. This, in turn, helps the company to improve the performance and increase the value of the company (Jensen & Meckling, 1976). Among the primary mechanisms providing the overseeing function and is important in tackling agency issues, is the board of directors (Lefort & Urzua, 2008).

The board of directors debatably plays a key role in safeguarding the shareholders' interests from various self-management interests. The most suitable solution to some agency problems in the current organisations is found in the board of directors' function (Hermalin & Weisbach, 2003).

The primary goal of the board is to reduce agency costs, increase disclosure of information that serves the stakeholders, and work to increase the shareholder's interests (Fama & Jensen, 1983). According to Abdullah (2004) and Andres, Azofra and Lopez (2005), the role of the board can be improved through the formation of the board, its size and its structure, which may help to increase performance to come up with strategic plans and implement them in the required manner.

On the other hand, the principal function of resource dependence theory is to interconnect a board with the external environment and to provide companies with eligible cadres,

who have high expertise and advanced degrees to help the company in dealing the external and internal environment. This in turn helps the company to achieve the objectives and improve its performance. Thus, the theory is always seeking to achieve a real partnership between all parties in order to provide the company with visions that always help to improve the company's performance (Pfeffer, 1972).

In addition, resource dependence theory suggests that in the business environment, there are a great number of external factors, which may give rise to uncertainty and external dependencies (Daily *et al.*, 1999). In the same vein, firms should deal with those uncertainties-generating factors to succeed in the competitive environment. Directors serve as liaisons between the firm and those uncertainties-generating external factors and help firms deal with those factors and make better investment decisions.

Specifically, the board's function is to obtain firm resources on the basis of the relationships the board members have developed with the other firms (Pfeffer, 1972; Provan, 1980; Zald, 1967). It is through the resource acquisition that the members of the board can minimise the degree of environmental uncertainty of the firm (Burt, 1983; Pfeffer, 1972; Thompson, 1967). Moreover, the role of the board encapsulates its ability to legitimize the organisation and develop boundary spanning opportunities to relate the interests of the firm with its counterparts (Dooley, 1969; Pennings, 1980). The board is also a source that contributes invaluable information regarding the way strategic decisions reached by the firm (Westphal & Fredrickson, 2001).

Hypothetically, the board has to bear all responsibilities for the company's operations its financial viability and ensure that it meets the requirements of the company and the interests of shareholders and the board plays a vital role in affecting the firm's financial performance (Coles & Jarrell, 2001; Fama & Jensen 1983). Past empirical studies revealed that the relationship between determinants of CG and FP has inconclusive results, as extensively discussed and explained in the previous chapter.

The current study attempts to consider the relationship between the determinants of CG namely, board of directors' characteristics (board size, board independence, board meeting, board change, secretary role, legal counsel and foreign member on the board), audit committee characteristics (size, independence and meeting), executive committee and firm performance (ROA and Tobin-Q) in Muscat Securities Market (MSM).

Based on the problem statement, there are identified theoretical gaps in the literature review. This study attempts to achieve its objectives and answer its questions through the research framework depicted in Figure 4.1.

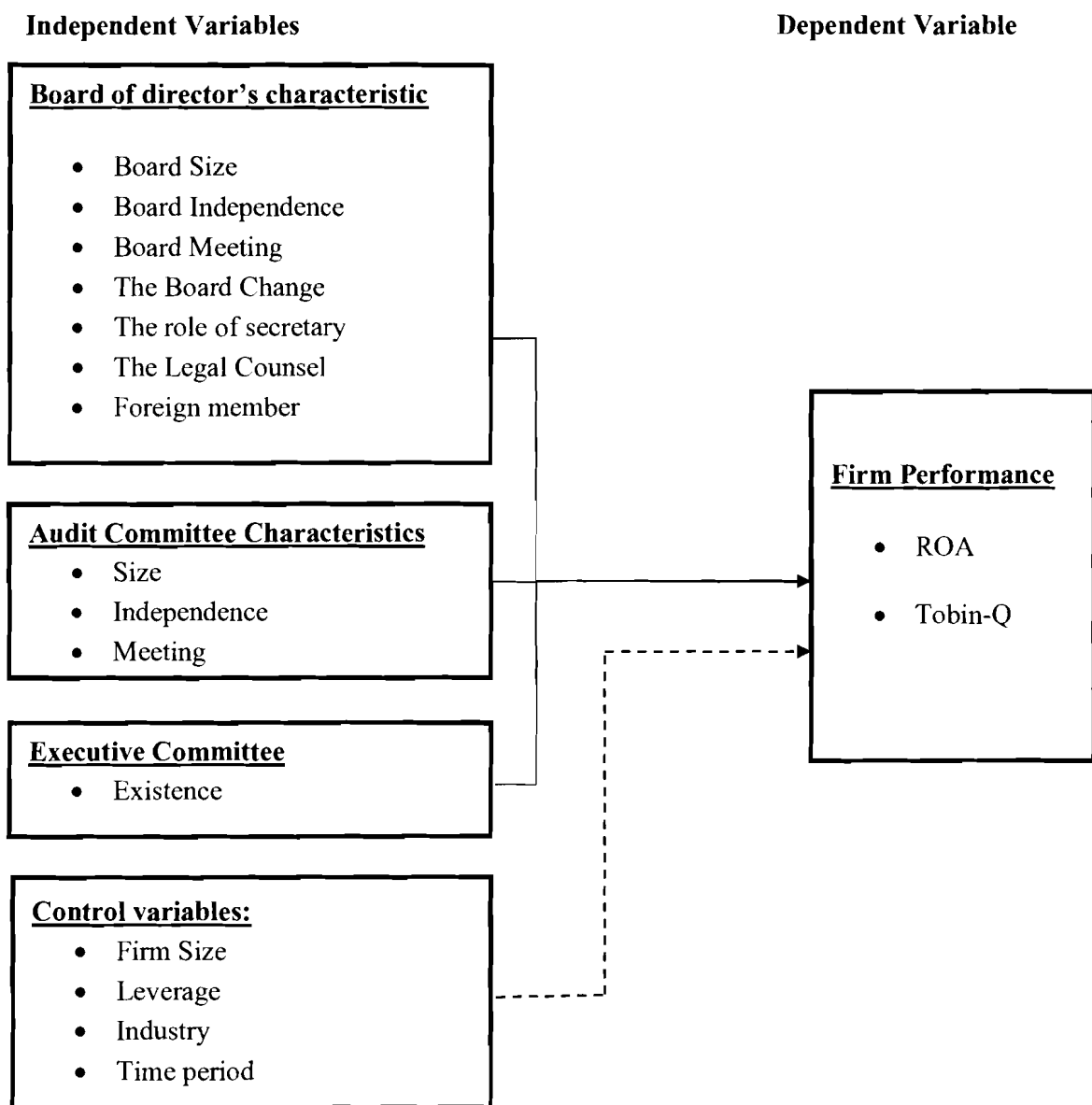


Figure 4.1
Research Framework

4.3 Hypotheses Development

The present section discusses the relationship between firm performance through ROA and Tobin Q as the dependent variable, and the corporate governance, including board of

directors' characteristics (board size, board independence, board meeting, board change, secretary role, legal counsel and foreign member on the board), audit committee characteristics (size, independence and meeting) and executive committee.

4.3.1 Firm Performance

The independent variable of the present study is the firm performance with the firm performance indicators represented by the return on asset (ROA) and Tobin-Q. The current study focuses on testing the firm performance by using two famous and common proxies of performance, accounting base measurement and market based measurement, the ROA and Tobin-Q. As majority of previous studies have used this proxy of performance (Al-Matari *et al.*, 2012a; Ibrahim & Abdul Samad, 2011; Herly & Sisnuhadi, 2011; Karaca & Ekşi, 2012; Liang, Lin and Huang, 2011; Lin, 2011; Najid & Abdul Rahman, 2011; Shahab-u-Din & Javid, 2011). It is important to state that this study employs two financial ratios (ROA and Tobin-Q) to measure the firm's performance because each one of them has advantages as discussed.

4.3.1.1 ROA

The accounting-based ROA is the firm measurement and ROA is different in various companies representing measurements of efficient utilisation of assets. It is generally an effective firm profitability indicator compared to a benchmark rate of return equivalent to the risk adjusted weighted average cost of capital (Al-Matari *et al.*, 2012a).

Additionally, the profit measures have been criticised as backward-looking and only partially estimating future events through depreciation and amortisation. The accountant, limited by standards laid down by the profession, gauges the rate of profit and hence, it is impacted by the accounting practices, including various methods employed in the assessment of both tangible and intangible assets (Kapopoulos & Lazaretou, 2007).

The ROA also gauges the firm's performance in terms of its finance and operations (Klapper & Love, 2004). Therefore, the higher the ROA, the more effective is the use of assets to satisfy the shareholders' interests (Ibrahim & Abdul Samad, 2011).

On the basis of Miller's (1995) study, ROA is the representation of a measurement that gauges the complete efficiency of how the firm's assets are used for the production of net income from the operations of the firm. He added that ROA represents the effectiveness of management in appropriating capital as they may be efficient but are unable to use capital.

4.3.1.2 Tobin-Q

The second measurement is the market-based measurement, the Tobin's Q. It is a forward looking measurement reflecting the shareholders' expectations regarding future performance of the firm, which is based on past or current performance (Ganguli & Agrawal, 2009; Shan & McIver, 2011; Wahla *et al.*, 2012).

As a traditional measure, Tobin-Q measures the expected long-run firm performance (Bozec *et al.*, 2010) as opposed to the market value of equity that measures the firm's growth opportunities arising from factors external to managerial decisions. This is exhibited through the company's level (Shan & McIver, 2011; Demsetz & Villalonga, 2001).

Tobin-Q is acknowledged as a superior measure of the performance of the firm (Mayer, 2003; Amran & Che-Ahmad, 2009). Similarly Ang and Ding (2006) and Najid and Abdul Rahman (2011) stated that Tobin-Q is a more stable way to provide an estimation of the firm value, as the value of the firm's assets are not as volatile as its share price when valuation proxies like book value or price to earnings are utilised.

The higher the Q value, the more effective will be the company's governance mechanisms. Tobin-Q also presents that the market's perception of the performance of the firm is good (Ibrahim & Abdul Samad, 2011; Weir *et al.*, 2002). The High Tobin-Q ratio is also a representation of success in terms of firm's deployment of investment for the benefit of the company that has more weight compared to its book value (Kapopoulos & Lazaretou, 2007).

The calculation of Tobin-Q in the current study is the result obtained from the market value of equity added to the book value of the debt over the book value of the total assets; a calculation utilised by Al-Matari *et al.* (2012b), Kang and Kim (2011), Karaca and Ekşi (2012) and Wahla *et al.* (2012) because it is difficult to get the required information

relating to the market value of debt issued such as the replacement cost of all assets by Omani firms, since these are not usually disclosed in their financial reports.

As the current study covers the board structure dimensions of corporate governances, it is good to use both measurements (ROA and Tobin-Q) because the integration between them reflects firm performance. In the same context, the results show that firms are better performing in terms of accounting and market performance as their stock returns exhibit more firm-specific information (Liang *et al.*, 2011; Ting, 2008). While Demsetz and Villalonga (2001) claimed that both measurements of performance have their disadvantages, their researchers stated that measurement of reliability can be increased by using both measurements to develop a composite measure of the financial performance of the firm (Gentry & Shen, 2010; Rowe & Morrow, 1999; Schwab, 1999). Based on the above discussion and recommended by Al-Matari *et al.* (2012a), both measurements should be utilised for CG and this is the reason why the present study does so.

There are previous empirical studies conducted based on accounting profitability and Tobin-Q, including Bhagat *et al.*, (2011), Heenetigala and Armstrong (2011), Herly and Sisnuhadi (2011), Karaca and Ekşi (2012), Liang *et al.* (2011), Lin (2011), Lin *et al.*, (2011), Najid and Abdul Rahman (2011), Obiyo and Lence (2011) and Shahab-u-Din and Javid (2011) as provided earlier in the literature review chapter. For this reason, the current study is consistent with the prior studies.

The present study concentrates on the independent variables, including board of directors' characteristics (board size, board independence, board meeting, board change, secretary role, legal counsel and foreign member on the board), audit committee's characteristics (size, independence and meeting) and executive committee. The contemporary section provides a discussion of these variables, which helps in reaching accurate findings. The objective investigates these variables as an effect on firm performance. The next section explains the related independent variables and the dependent variable in detail.

4.3.2 The Board of the Directors Characteristics and Firm Performance

4.3.2.1 The Board Size and Firm Performance

The size of the board is considered to affect the strength of its monitoring. In other words, the larger the board, the more capable it is to monitor top management (Abdullah, 2004). The size of the board is a representation of the number of directors occupying seats in the corporate board. The board of directors is generally considered the core of corporate governance mechanisms and is the basic means for shareholders to control top management indirectly (John & Senbet, 1998).

On the other hand, Lipton and Lorsch's (1992) study revealed that as the size of the board increases, monitoring management turns less effective. They stated that the ideal board size should be between eight and nine members and any extra benefits from the increased monitoring of the extra members will counteract the costs linked with slow decision

making and to the expended efforts. This is consistent with Jensen's (1993) contention that the board of directors is less effective when their numbers are more than seven or eight members.

Along the same line, Jensen (1993) also revealed that large boards are not as effective as smaller ones and the members' discussions may not be as meaningful. Increased board size corresponds to difficulties arising in coordination and processing of issues. Shaver (2005) mirrors the same statement by saying that larger boards primarily show issues of responsibility diffusion leading to social loafing and urging the fractionalisation of the group and the reduction of the members' commitment to strategic change.

Moreover, larger boards are inefficient in terms of higher spending on the maintenance and report more difficulties in terms of planning, work coordination, decision making and having regular meetings because of the number of members. On the other hand, smaller boards are ideally capable to avoid free riding by directors and encourage the efficient decision making process.

Viewed from another perspective, the board function is the acquisition of the resources of the firm, based on its members' relationship with other firms (Pfeffer, 1972; Provan, 1980; Zald, 1967). Therefore, it is the reason that more members of the board or a larger board size would result in better corporate performance owing to pool of various skills, knowledge and expertise that are presented to the boardroom. Moreover, larger boards are more proficient to provide the diversity that would assist firms in securing invaluable

resources and reducing environmental uncertainties (Goodstein *et al.*, 1994; Ghazali, 2010; Pearce and Zahra, 1992; Pfeffer, 1987).

Furthermore, the bigger the board is, the more is the possibility that the stakeholders' interests are considered and the less likely that decisions will be reached in favour of only a few members (Shao, 2010). According to Pfeffer and Salancik (1979), larger boards are more capable to obtain invaluable resources including budgeting, funding and leveraging the external environments which lead to the improvement of the performance of the firm.

Although there are empirical evidences regarding the effect of board size on firm performance, yet the findings are still mixed. The previous studies in the developed countries are consistent with the agency theory by confirming that there is a negative relationship between board size and firm performance. These studies include Ben-Amar and Andre (2006), Florackis (2005), Gavrea and Stegorean (2012), Irina and Nadezhda (2009), Juras and Hinson (2008), Liang, Xu, and Jiraporn (2013), Nanka-Bruce (2011), O'Connell and Cramer (2010) and Yawson (2006). Similarly, in the developing countries, many studies found the relationship between the board size and firm performance to be negative (Al Farooque *et al.*, 2007; Al Manaseer *et al.*, 2012; Ali & Nasir, 2014; Al-Najjar, 2014; Amran & Che-Ahmad, 2009; Chechet, Jnr & Akanet, 2013; Garg, 2007; Haniffa & Hudaib, 2006; Ibrahim & Abdul Samad, 2011; Kota & Tomar, 2010; Lin, 2011; Mashayekhi & Bazazb, 2008; Mollah & Talukdar, 2007).

In the light of the resource dependence theory, many studies in the developed countries have found that the relationship between board size and firm performance is positive (Bauer *et al.*, 2009; Fairchild & Li, 2005; Galbreath, 2010; Juras & Hinson, 2008; Khanchel, 2007; Larmou & Vafeas, 2010; Premuroso & Bhattacharya, 2007; Sueyoshi *et al.*, 2010). In the same line of similar outcome, but different countries, a positive relationship is found between board size and firm performance in the developing countries. This is evident in the studies conducted by Abdullah *et al.* (2008), Al-Najjar (2013), Black *et al.* (2003), Chahine and Safieddine (2011), Chang (2009), Chugh *et al.* (2011), Chung *et al.* (2008), Danoshana & Ravivathani (2014), Dar *et al.* (2011), Dwivedi and Jain (2005), Ehikioya (2009), Haniffa and Hudaib (2006), Hsu and Petchsakulwong (2010), Ibrahim *et al.* (2010), Jackling and Johl (2009), Kajola (2008), Kamardin (2009), Kang and Kim (2011), Khan and Javid (2011), Kyereboah-Coleman (2007), Kyereboah Coleman and Biekpe (2006), Li, Kankpang and Okonkwo (2012), Mehraban and Dadgar (2013), Najjar (2012), Obiyo and Lenee (2011), Sahu and Manna (2013), Saibaba and Ansari (2013), Sheikh, Wang and Khan (2013), Swamy (2011), Uadiale (2010), Yasser, Entebang and Mansor (2011) and Zainal Abidin, Kamal and Jusoff (2009). A detailed summary of the studies regarding this relationship is provided in Chapter Three.

Apart from both the agency theory and resource dependence theory, some evidences have been revealed that no association exists between firm performance and board size in the developed nations (Belkhir, 2005; Bhagat & Bolton, 2008; García-Sánchez, 2010;

Herrmann *et al.*, 2010; Kiel & Nicholso, 2006; Lehn *et al.*, 2009; Millet-Reyes & Zhao, 2010; Shao, 2010; Siala *et al.*, 2009; Wei, 2007) and in the developing countries (Abdurrouf, 2011; Aljifri and Moustafa, 2007; Al-Matari *et al.*, 2012; Al-Matari *et al.*, 2012b; Al-Najjar, 2013; Bektas & Kaymak, 2009; Belkhir, 2005; Chiang & Lin, 2011; Dar *et al.*, 2011; Ghabayen, 2012; Ghazali, 2010; Guoa & Kgab, 2012; Ibrahim & Abdul Samad, 2011; Ibrahim *et al.*, 2010; Kajola, 2008; Kamardin, 2009; Kula, 2005; Kyereboah-Coleman & Biekpe, 2006; Kyereboah-Coleman, 2007; Latief, Raza & Gillani, 2014; Lin, 2011; Noor, 2011; Nuryanah & Islam, 2011; Prabowo & Simpson, 2011; Rachdi & Ameer, 2011; Stanwick & Stanwick, 2010; Vo & Nguyen, 2014). On the basis of the previous discussion and supporting arguments, the following hypotheses are developed;

H₁: There is a relationship between board size and firm performance.

H_{1a}: There is a relationship between board size and ROA.

H_{1b}: There is a relationship between board size and Tobin-Q.

4.3.2.2 Board Independence and Firm Performance

Board independence is another measurement of the board characteristics' quality, which has caught the attention of researchers and practitioners alike. The independence of the board refers to the number of independent non-executive members positioned in the board relative to the total number of members (Lawal, 2012; Uadiale, 2010).

According to the Omani Code of Corporate Governance (2002), it is mandatory that at least three members should be non-executive directors and the board should comprise of the majority non-executive directors as board independence has a key role (Lin, 2011). Specifically, the role of independent directors on the board is to provide effective monitoring and control of firm activities and hence, to reduce the managerial opportunistic behaviours along with the expropriation of the assets of the firm (Abdurrouf, 2011; Pandya, 2011).

Similarly, the board's independent directors can work independent of the control or influence of the major shareholders, management or other parties. This means they are more likely to supervise management and prevent fraud, as they do not have any economic or psychological links with management (Hsu & Petchsakulwong, 2010).

Moreover, according to Fama and Jensen (1983) external directors are more conscientious about their reputations and social statuses, which propel them to oversee management and guarantee the company's effective running. Furthermore, the board independence also assists in reducing agency problem and this is the reason why shareholders often try to replace inside directors with external directors for better management monitoring (Hermalin & Weisbach, 1991; Weisbach, 1988). Daily (1995) also suggested that external directors are more capable of providing a superior level of objectivity when assessing the situation of the firm – a contention supported by Coughlan and Schmidt (1985) who stated that external directors are more superior monitors and are considered as an invaluable disciplining mechanism for managers.

It is further argued that board having more independent directors may minimise management's opportunistic behaviour and in essence safeguard the interests of shareholders more effectively as compared to their dependent counterparts (Chaghadari, 2011; Zainal Abidin, Kamal & Jusoff, 2009).

Generally, all CG practices around the world suggest that an independent member should be included on the board (Nuryanah & Islam, 2011). Independent directors can minimise the agency cost as it makes the monitoring role and the strategic planning role of the board more effective (Berle & Means, 1932).

In view of CG, the agency theory indicates that sufficient monitoring mechanisms employed to safeguard shareholders from the self-interests of management. Hence, a high number of external directors on the board is considered as having a potential positive impact upon performance (Fama & Jensen, 1983; Jensen & Meckling, 1976; Shleifer & Vishny, 1997).

On the other hand, consistent to resource dependence theory, the outside sources provide a firm with external channel to improve performance. The independent board enables board members to better understand complex environments and give multiple knowledge and experience from different sources to improve the firm performance (Pfeffer, 1972).

With regard to the agency theory and resource dependence theory, the relationship between board independence and firm performance is supposed to be positive. In general, so many studies have shown a positive impact on the board composition upon

performance in the developed and developing countries. Many researchers have investigated into the relationship in the developed countries such as, Bhagat and Bolton (2009), Bozec *et al.* (2010), Chamberlain (2010), Dey (2008), Galbreath (2010), Harjoto and Jo (2008), Heenetigala and Armstrong (2011), Juras and Hinson (2008), Lehn *et al.* (2009), Liang, Xu, and Jiraporn (2013), Mahadeo *et al.* (2012), Müller (2014), Nanka-Bruce (2011), O'Connell and Cramer (2010), Premuroso and Bhattachar (2007), Reddy *et al.* (2010), Saibaba and Ansari (2011) and Shan and McIver (2011). Many researchers in the developing countries also have been getting a positive relationship between the board independence and firm performance by Abdurrouf (2011), Al Manaseer *et al.* (2012), Ali and Nasir (2014), Al-Najjar (2013), Al-Najjar (2014), Azam *et al.* (2011), Bozcuk (2011), Chechet, Jnr and Akanet (2013), Chiang and Lin (2011), Cho and Kim (2007), Choi *et al.* (2007), Hsu and Petchsakulwong (2010), Ibrahim and Abdul Samad (2011), Kang and Kim (2011), Khan *et al.* (2011), Li *et al.* (2012), Mashayekhi and Bazazb (2008), Nuryanah and Islam (2011), Obiyo and Lenee (2011), Swamy (2011), Uadiale (2010), Yasser *et al.* (2011) and Zainal Abidin, Kamal and Jusoff (2009).

Contrariwise, since inside directors spend their lives working in the firm, they have a better understanding of the firm's businesses so that they can make better decisions (Donaldson, 1990). With that in mind, the relationship between the board independence and firm performance should be negative. First, a negative relationship was found between board independent and firm performance in developed countries such as Bhagat and Bolton (2008), Bozec (2005), Firth *et al.* (2006), Irina and Nadezhda (2009), Jermias

and Gani (2014), Pan, Lin and Chen (2013), Singh and Gaur (2009), Stanwick and Stanwick (2010), Switzer and Tangb (2009), Valenti *et al.* (2011) and Wang and Oliver (2009). A similar finding was reported in the developing countries such as in the studies by Bektas and Kaymak (2009), Chahine and Safieddine (2011), Chang (2009) Ghabayen (2012), Noor (2011) and Khan and Javid (2011), Sahu and Manna (2013), Sheikh, Wang and Khan (2013) and Vo and Nguyen (2014).

The relationship between board independence and firm performance was found to be non-significant in both the developed states in studies such as Adjaoud *et al.* (2007), Belkhir (2005), Bøhren and Strøm (2010), García-Sánchez (2010), Hu *et al.* (2010), Siala *et al.* (2009), Wei (2007) and Yue *et al.* (2008) and developing nations like Al-Matari *et al.* (2012), Chaghadari (2011), Chowdhury (2010), Chugh *et al.* (2011), Ehikioya (2009), Ghazali (2010), Guoa & Kgab (2012), Ibrahim and Abdul Samad (2011) , Ibrahim *et al.* (2010), Kajola (2008), Kota and Tomar (2010), Kumar and Singh (2012), Kyereboah-Coleman (2007), Al- Matari *et al.* (2012b), Noor (2011), Pandya (2011), Prabowo and Simpson (2011), Rachdi and Ameer (2011) and Sahu and Manna (2013). Based on the theoretical perspective and debate above, the following hypotheses are expressed:

H₂: There is a positive relationship between board independence and firm performance.

H_{2a}: There is a positive relationship between board independence and ROA.

H_{2b}: There is a positive relationship between board independence and Tobin-Q.

4.3.2.3 Board Meeting and Firm Performance

Board meeting refers to the number of meetings held by the board on a yearly basis. With regards to the Omani Code of Corporate Governance (2002), it is mandatory for the board to hold 4 meetings in a year with a maximum gap of 4 months between two consecutive meetings. Prior studies focused on two factors of board characteristics, which are board size and board independence. This research, however, adds the board meeting variable (Al Manaseer *et al.*, 2012; Kang & Kim, 2011; Li *et al.*, 2012; Nanka-Bruce, 2011; Obiyo & Lenee, 2011) as it has become vital to companies. Board meetings are important because boards hold meetings on behalf of the company and there is a process entailing the board's collective action, which includes passing of resolution on board meetings. More meetings mean more chances of considering different decisions by the boards and quickly reaching final results (Khan & Javid, 2011).

The board effectiveness depends on the frequency of its meetings as this can enhance the performance of the firm, given the fact that the board provides with more opportunity of monitoring and reviewing the performance of management (Hsu & Petchsakulwong, 2010). This is consistent with Evans *et al.*, (2002) and Hsu and Petchsakulwong's (2010) findings that revealed that the board of directors often increase the frequency of its meetings in order to find solutions to problems concerning declining firm performance.

Jackling and Johl (2009) and Lipton and Lorsch (1992) also claimed that the more frequent the meetings, the more likely a superior performance can be achieved. Similarly,

Conger *et al.* (1998) and Kyereboah-Coleman (2007) stated that board meeting time is a critical resource used to improve the corporate board's effectiveness, indicating that with frequent meetings the board is more likely to improve the performance of the firm and perform duties according to the interests of the shareholders (Kyereboah-Coleman, 2007).

Vafeas (2000) also stated that frequency of board meetings is a significant activity because as the board meetings increase in frequency, the more the firm will improve its operating performance. Thus, boards should be inclined to increase frequency of meetings if the situation calls for high control and oversight (Khanchel, 2007; Shivdasani & Zenner, 2002).

Furthermore, the intensity of board activity (measured by meetings frequency) is one aspect of the resource dependent theory that is related to corporate governance and performance. Regarding the resource dependence theory, board meeting helps the board to valuate and pursue a board business time by time and to solve any problem faced by employees (Pearce & Zahra, 1992; Pfeffer, 1987). Hence, the board meeting frequency may help in increasing the performance of a firm.

On the other hand, it was argued by Jensen (1993) that daily tasks those constitutes most of the board's meeting time and hence this limits the chances for external directors to conduct a meaningful oversight over management. Jensen (1993) suggested that boards should not be very active as board activity represents a reaction to adverse performance. In addition to that, Jackling and Johl (2009) revealed that the board's reaction to poor

performance by increasing board of activity which is in turn, related with enhanced operating performance in the coming years which indicates a lag effect. Rebeiz & Salame (2006) also emphasised on the quality of the board meeting as opposed to frequency.

Due to the importance of board effectiveness on firm performance variation, studies have been conducted to study this relationship in developed as well as developing countries. The relationship between board meetings and firm performance was reported to be positive in the developed countries (Gavrea & Stegorean, 2012; Khanchel, 2007; Liang, Xu, & Jiraporn, 2013; Lin *et al.*, 2002) and in the developing countries such as, Sahu & Manna (2013), Khan and Javid (2011), Kang and Kim (2011), Hsu and Petchsakulwong (2010) and Kamardin (2009). While some studies have confirmed the negative effect of the board meeting on firm performance in both developed such as García-Sánchez (2010) and Qinghua *et al.* (2007) and developing countries (Danoshana & Ravivathani, 2014; Kamardin, 2009; Noor, 2011). Some studies found that there is no significant relationship between board meetings and firm performance (Gavrea & Stegorean, 2012; Kyereboah-Coleman, 2007; Noor, 2011). Based on the above discussion, it is reasonable to hypothesise the following hypotheses.

H₃: There is a relationship between the number of board meetings and firm performance.

H_{3a}: There is a relationship between the number of board meetings and ROA.

H_{3b}: There is a relationship between the number of board meetings and Tobin-Q.

4.3.2.4 Board Change and Firm Performance

The board of directors is critical monitoring mechanism that oversees management performance and protects the interests of shareholders (Fama & Jensen, 1983). The board change is defined to be the appointment of a new member on the board during a year (Fox & Opong (1999)).

The objective behind the board change is to give new blood to the board to make them more active to fulfil their tasks. The board members' main target is to achieve the shareholder's target and at the same time to achieve the target of the owners. So, the agency theory postulates that the board is responsible to monitor and improve performance (Fama & Jensen, 1983). On the other hand, from the perspective of resource dependence theory, variety of members provides multiple knowledge and experience, which enhance performance (Pfeffer, 1972). Hence, this current study expects board change to improve firm performance.

According to Fox and Opong (1999), board composition changes could benefit the firm for many reasons. Firstly, all the directors on the board possess the authority to influence the firm's policies and objectives and thus, the firm performance. A new member of the board may bring a novel and dynamic outlook to the firm operations. In addition, extensive experience and knowledge can also be brought in by the appointment of qualified and experienced executives. Secondly, replacing an ineffective member indicates that the firm is in the process of initiating procedures and actions that will

enhance the firm's efficiency that will lead to the enhancement of firm performance. As an individual member's potential contribution to the board is inconspicuous, the performance of a firm's share price can be considered as an indirect measure of the information included in the change in the board's composition.

More specifically, no known study so far has examined this relationship in the developing countries in general and in Oman in particular. Hence, the present study accounts for two important contributions. First, it examines the impact of firm board changes upon firm performance in Oman and second, unique to itself, it is the pioneering study to examine the board change-firm performance (ROA & Tobin-Q) relationship.

Further examination of this relationship is suggested by some researchers such as Al-Matari *et al.* (2012a). More specifically, they encouraged future researchers to study the effect of some variables such as the board change, the role of secretary on the board and the executive committee on firm performance. From this recommendation, the current study is the first study (to the knowledge of the researcher) to examine the association between board change, the role of secretary on the board and the role of the executive committee with firm performance. The study expects board change and the executive committee to improve performance of companies.

Finally, the importance of the board change is that it gives new blood to the directors with consistent multiple experiences, knowledge and innovative thoughts with more motivation. This study is going to fill the existing gap and consider testing this variable

with firm performance. Based on the previous arguments and others supporting arguments, the following hypotheses are formulated:

H₄: There is a relationship between the board change and firm performance.

H_{4a}: There is a relationship between the board change and ROA.

H_{4b}: There is a relationship between board change and Tobin-Q.

4.3.2.5 The Role of Secretary on the Board and Firm Performance

A company secretary often holds a senior position in the private or public sector companies in the management echelons. In the context of large American and Canadian publicly listed firms, a company secretary is often referred to as a Corporate Secretary or the Secretary. He/she is responsible for the administration of the company specifically when it comes to making sure that the company adheres to the statutory and regulatory requirements and to ensure that the decisions of the board are carried out (general theory). This study expects the role of secretary on the board to contribute to the effective performance of the firm through the organisation of the board tasks.

Moreover, the company secretary is the legal representative in the firm documents; it is the secretary's responsibility to make sure that the company, and its directors' activities are consistent with the law. The secretary is also responsible for registering and communicating with shareholders, to guarantee just payment of dividends, and to maintain the records of the company with the inclusion of the lists of directors and shareholders, and the annual accounts (Murray, 1982). In most developed countries, law

to elect one person as the secretary of the company often mandates private companies and he/she is usually a senior member of the board.

Regarding the agency theory postulation, the separation of two positions in the company helps improving and increasing the protection of the rights of shareholders (Jensen & Meckling, 1976). From the perspective of resource dependence theory, the splitting up of two positions in the company may not assist in improving the value of shareholders (Pfeffer & Slanick, 1979). Hence, the current study supposes that the role of secretary on the board improves firm performance.

The role of the secretary of the board is to arrange all board activities and to give a clear picture about what they discussed and what they should do. The current study expects the significance of this variable to board structure. Al-Matari *et al.* (2012) also suggested the importance of secretary of the board to the firm performance. Based on the theoretical and previous discussion, the following hypotheses are reasonable to be proposed for further empirical investigation.

H₅: There is a relationship between the role of secretary on the board and firm performance.

H_{5a}: There is a relationship between the role of secretary on the board and ROA

H_{5b}: There is a relationship between the role of secretary on the board and Tobin-Q.

4.3.2.6 The Legal Counsel and Firm Performance

The influence of the legal profession upon board structure is still partially ambiguous. Initiatives have been launched for its extensive investigation but questions still prevail of what describes board composition (Rose, 2006).

Firms may employ external directors during performance decline for their novel ideas and the knowledge pool or even to indicate that the operations are in the process of improvement (Pearce & Zahra, 1992). According to Davis and Thompson (1994), the appointment of external directors may also be prompted by the threat of lawsuits. From this point of view, the study considers legal counsel as a variable.

Additionally, many assumptions have been brought forward regarding the board independence in some European capital markets. However, some of these assumptions highlighted the unresolved issue of whether the change in board composition is for the shareholders' benefit or for the reduction of transaction costs. Hence, an extensive examination to resolve the question of what constitutes the board composition may be able to guide future work in this topic and it may support the impact of legal counsel on the board upon firm performance (Juras & Hinson, 2008).

The role of legal counsel in the firm is very essential to mitigate judicial allegations. It is expected to give a firm, clear insight into future contracts with investors. It is also expected to solve any problem related to the legal system. The separation of the jobs

provides power to make the right decisions and to directly monitor management procedures, which would eventually lead to better performance (Al Busaidi, 2008).

In the light of the resource dependence theory, the external source will give a firm countless experience and knowledge to deal with the transaction experienced during the life cycle (Rao *et al.*, 2007). The legal counsel can align the firm with the legal system all the time without any problems. Regarding to the Omani Code of Corporate Governance (2002), the firm should have legal counsel to revise any transaction according to the legal system. For example, the legal code inside the firm governs the relationship between the firm and investors to solve any local or foreign issues. Additionally, the legal counsel tries to plead for the company in the presence of the company's rights to third parties.

Given the importance of legal counsel as an important code of CG, and literature's contention of its negligence, in the present study it is considered as a variable. The role of the legal counsel on the firm performance was suggested to be investigated by Al-Matari *et al.* (2012). Based on previous arguments and supporting ones, the following hypotheses are proposed to be empirically tested;

H6: There is a relationship between the legal counsel and firm performance.

H_{6a}: There is a relationship between the legal counsel and ROA.

H_{6b}: There is a relationship between the legal counsel and Tobin-Q.

4.3.2.7 Foreign Member on the Board and Firm Performance

The series of accounting scandals that occurred in the recent times has led the investors to concern about the organisations' governance. The fall of once considered 'unsinkable' companies like Enron and WorldCom in the US, and Ansett, OneTel and HIH in Australia has urged investors and stakeholders to demand superior CG, particularly for the purpose of 'cleaning up' the board room (Cheng, 2003; Houle, 1990; Park & Shin, 2003).

The diversity of the board is described as variety in the board of directors' independence. There are two types of diversity, namely the observable and the non-observable type. The former includes gender, age, race and ethnicity while the latter includes knowledge, education, values, perception, and characteristics of personality (Boeker, 1997; Erhardt, Werbel & Shrader, 2003; Kilduff, Angelmar & Mehra, 2000; Maznevski, 1994; Milliken and Martins, 1996; Pelled, 1996; Petersen, 2000; Timmerman, 2000; Watson, Kumar & Michaelsen, 1993). Majority of diversity studies and its impact upon performance concentrate on the demographic type of diversity.

The diversity of directors on the board improves information accessibility and the processing capacity of the firm that allow board members to comprehend the complex dynamic environments, to examine a larger number of solutions and eventually to generate effective decisions. Furthermore, the diversity of the board is a crucial element of the successful board and strategic control role. Moreover, the board diversity can be

measured through the foreign member on the board, gender and age. The focus of this study is on the foreign member on the board because these famous factors reflect the performance of firms and the easiness to get data from the companies and the reason to choose these elements is their increasing importance and accessibility (Kim, Burns & Prescott, 2009).

The foreign directors take along with them valuable knowledge related to contextual issues in international markets and are enabled to maximise the strategic decision-making quality (Zahra & Filatotchev, 2004).

In the light of the resource dependence theory, the foreign directors inside the firms give a lot of foreign experiences and foreign knowledge which help firms to solve any problem inside multinational firms and to help employees to deal with foreign problems if any (Pfeffer & Salancik, 1979).

There are mixed results concerning the link between foreign member and firm performance. Evidence provided by Miletkov *et al.* (2011) revealed a negative impact between international directors and firm performance. Contrarily, Ruigrok *et al.* (2007) found an association between nationality (foreign) and gender and the corporate board. Moreover, the foreign member on the board is to improve performance of the company. Although the importance of this variable is evident, yet there is lack of previous studies examining this relation. Some recommendations were made by Al-Matari *et al.* (2012)

and Kang, Cheng and Gra (2007) to examine this relationship. This study contributes to literature by testing the following hypotheses.

H₇: there is a relationship between foreign member on the board and firm performance.

H_{7a}: There is a relationship between foreign member on the board and ROA

H_{7b}: There is a relationship between foreign member on the board and Tobin-Q.

4.3.3 Audit Committee Characteristics and Firm Performance

In the present section, the impact of three critical audit committee characteristics (ACC) factors upon performance is extensively discussed. Audit is the bridge that joins the communication network between auditors (internal and external). Those are responsible for reviewing the nomination of auditors, the complete audit scope, the audit results, internal financial controls and financial information for publication (Chanawongs *et al.*, 2010). In the same context, the presence of audit committee serves as an important monitoring device to control management activities that lead to increase the firm's performance (Rahmat *et al.*, 2009; Xu *et al.*, 2005).

Additionally, an audit committee can support the board in implementing, monitoring and continuing good corporate governance practices benefitting the firm and its stakeholders (Saibaba & Ansari, 2011). Furthermore, Forker (1992) viewed the presence of the audit committee as an indication of the improvement of internal control and a monitoring

mechanism for enhancing firm value (Kim & Yoon, 2007). Finally, the integration of these three reflects and improves performance of the company.

4.3.3.1. Audit Committee Size and Firm Performance

The audit committee size is one of the commonly discussed elements of ACC. It is measured by the number on the audit committee serving on the firm (Bauer *et al.*, 2009; Hsu & Petchsakulwong 2010; Nuryanah & Islam, 2011; Obiyo & Lenee 2011).

With regards to the agency theory, the management-shareholders conflict often leads to top management's decision to serve their own interests and not the shareholders, particularly when management is a very opportunistic person (Jensen & Meckling, 1976). In the absence of independent and effective control procedures, top management is often inclined to go against protecting the interests of shareholders (Fama & Jensen, 1983). Therefore, audit committees that are efficient and effective must be able to resolve conflicts (Klein, 2002) and to work towards sustainable good performance (Charan, 1998; Rahmat *et al.*, 2009).

To boot, a larger audit committee could offer stricter monitoring, but it makes conclusions difficult to reach (Hsu & Petchsakulwong, 2010). The quality of the audit committee is basically related to the corporate board's quality which is its origin; board structure has also been cited by policy makers and academics as a determinant of financial statement quality (Pagano, Schwartz, Wagner & Marinelli 2002; Vafeas, 2005). By the same token, Dalton *et al.* (1999) found too small or too large audit committees to

be ineffective. A large one is more inclined to lose focus and to be more complacent than a smaller one.

According to the resource dependence theory, the larger the audit committee, the better will be the firm performance. A small audit committee does not possess the same diversity of skills and knowledge as its larger counterpart and therefore, becomes ineffective. An ideally sized audit committee offers members the opportunity to use the different experiences and expertise for the stakeholders' interests (Pearce & Zahra, 1992; Pfeffer, 1987). Although the relationship between the audit committee size and performance has been discussed extensively in the literature, the results are still inconclusive. To the proponents of the agency theory, performance is expected to be poor when the size of the committee is big.

Many researchers around the world have examined the relationship between audit committee size and firm performance both in developed countries (Bozec, 2005) and developing countries (Al-Matari *et al.*, 2012b; Hsu & Petchsakulwong, 2010; Mollah & Talukdar, 2007). They confirmed the negative association between them.

On the other hand, some studies conducted in developed countries examined the relationship between audit committee size and firm performance and found it to be positive (Bauer *et al.*, 2009; Khanchel, 2007; Premuroso & Bhattacharya, 2007; Reddy *et al.*, 2010). Similar findings were found in some developing countries (Al-Matari *et al.*, 2012; Black & Kim, 2007; Black *et al.*, 2003; Danoshana & Ravivathani, 2014;

Heenetigala & Armstrong, 2011; Kyereboah-Coleman, 2007; Obiyo & Lenee, 2011; Swamy, 2011).

Apart from the agency theory and resource dependence theory, some studies found no relationship between the audit committee and firm performance, such as Abdurrouf (2011), Ghabayen (2012), Kajola (2008), Kim and Yoon (2007), Kyereboah-Coleman (2007), Noor (2011), Rahmat *et al.* (2009), Nuryanah and Islam (2011) and Wei (2007). Based on the past literature regarding their relationships, the following hypotheses are formulated:

H₈: There is a relationship between audit committee size and firm performance.

H_{8a}: There is a relationship between audit committee size and ROA

H_{8b}: There is a relationship between audit committee size and Tobin-Q.

4.3.3.2 Audit Committee Independence and Firm Performance

Audit committee independence is the second key element of ACC. It should have at least three members (directors) and two-third (2/3) of the members should be non-executive independent directors. The selection of the chairman is carried out among the autonomous non-executive directors and is appointed by the BOD. The audit committee independence is described as the proportion of the non-executive and executive directors (Kang & Kim, 2011; Abdullah *et al.*, 2008). The corporate governance principles state that audit committees should work independently and perform their duties in a professional manner. In situations of financial manipulation, the committee will be

accountable for their actions as the transparency in financial information leads to minimal information asymmetry and enhances firm value (Abdurrouf, 2011; Bhagat & Jefferis, 2002).

Audit committee characterised by a higher member of non-executive directors are considered more independent compared to those with more executive directors (Rahmat *et al.*, 2009). Similarly, external audit committee members have a key role in making sure the practices of corporate governance in auditing processes (Swamy, 2011). Moreover, according to Abdullah *et al.* (2008), firms having a majority of internal directors and lacking audit committee are more likely to take part in committing financial fraud compared to their controlled counterparts in a similar industry and with the same size.

From the perspective of both, the agency theory and resource dependence theory, the autonomy given provides the opportunity to reach the right decision without any restriction and to detect errors and reveal them without any problems because the independent reviewers are not related to the company. The relationship between audit committee independence and firm performance is anticipated to be positive. However, there are very few studies that have examined the relationship between audit committee independence and firm performance both in the developed nations (Dey, 2008; Khanchel, 2007) or the developing countries (Abdullah *et al.*, 2008; Chechet, Jnr & Akanet, 2013; Nuryanah & Islam, 2011; Saibaba & Ansari, 2011; Swamy, 2011; Yasser *et al.*, 2011). They found a positive association between the audit committee independence and firm performance.

Correspondingly, few researchers also found a negative association between the audit committee independence and the firm performance (Dar *et al.*, 2011). In the end, there are some researchers who found adverse results in prior outcome and revealed no relationship between audit committee independence and firm performance such as, Al-Matari *et al.* (2012a), Al-Matari *et al.* (2012b), Dar *et al.* (2011), Ghabayen (2012), Khan and Javid (2011), Kota and Tomar (2010), Kyereboah-Coleman (2007) and Rahmat *et al.* (2009). In light of the previous arguments and other supporting ones, the following hypotheses are proposed.

H₉: There is a positive relationship between audit committee independence and firm performance.

H_{9a}: There is a positive relationship between audit committee independence and ROA.

H_{9b}: There is a positive relationship between audit committee independence and Tobin-Q.

4.3.3.3 Audit Committee Meeting and Firm Performance

The meeting of the audit committee is among the widely investigated ACC and almost all prior researches utilise the meeting frequency as proxies for the activeness of the audit committee (Hsu & Petchsakulwong, 2010; Khanchel, 2007; Kyereboah-Coleman, 2007; Rahmat *et al.*, 2009).

Consistent with the suggestions of previous studies conducted by Hsu and Petchsakulwong (2010) and Kalbers and Fogarty (1993), the diligence of the audit committee is related to its effectiveness. Along the same line, Hsu and Petchsakulwong (2010) and Menon and Williams (1994) claimed that the frequency of meetings indicates diligence.

Additional to that, Abbott, Peters and Raghunandan (2003) stated that frequent meetings of the audit committee may lead to the improvement of the financial accounting processes which in turn, leads to superior performance. Sharing the same perspective is the resource dependence theory which stated that the board meeting helps the board to valuate and pursue the board business from time to time and to solve any problem encountered by employees (Pearce & Zahra, 1992; Pfeffer, 1987).

From another perspective, under agency theory, Jensen (1993) suggested that boards should be relatively inactive and evidence of higher board activity is likely to symbolise a response to poor performance. Likewise, Jackling and Johl (2009) and Lipton and Lorsch (1992) suggested that greater frequency of meetings is likely to result in superior performance. Moreover, Rebeiz and Salame (2006) argued that the quality of meetings is also important and that increasing the number of meetings does not necessarily enhance a firm's performance.

In general, a thorough review of the current literature shows that there is no clear-cut relationship between the board meeting and firm performance. There are few researchers

that have investigated this association and found a positive relationship between the audit committee meeting and firm performance in the developed countries, for example Khanchel (2007) and in the developing countries (Chechet, Jnr & Akanet, 2013; Kang & Kim, 2011; Kyereboah-Coleman, 2007; Saibaba & Ansari; 2013). Conversely, Hsu and Petchsakulwong (2010) found a negative relationship between the audit committee meeting and firm performance.

From another perspective apart from these two theories, no association was found between audit committee meeting and firm performance; for instance, Al-Matari *et al.* (2012a), Al-Matari *et al.* (2012b), Kyereboah-Coleman (2007), Noor (2011) and Rahmat *et al.* (2009).

Based on the conflict evident between the theories and past evidence, the results are still conclusive. Hence, the following hypotheses are formulated:

H₁₀: There is a relationship between audit committee meeting and firm performance.

H_{10a}: There is a relationship between audit committee meeting and ROA.

H_{10b}: There is a relationship between audit committee meeting and Tobin-Q.

4.3.4 The Executive Committee and Firm Performance

Due to the global financial crisis of recent times that toppled many of the global commercial entities, a very big lesson is learned by business entities that have been

affected and implemented appropriate strategies for risk management. Therefore, risk management has become one of the most important elements in the context of what the company is doing to generate revenue and maximise shareholder value while maintaining the economic stability of the country in which they are operating (Al Rashid & Jamal, 2010).

Also, CG has begun to look at the concept of risk management in a more serious light. Inconsistent with the risk-based approach, a board employing firm-wide risk management system increases the risk awareness of the firm which in turn, increases firm knowledge, thus enables the board to reach meaningful decisions and to create a positive effect on the governance structures and the firm's control environment. Effective CG has also been evolving from merely command-and-control statements to a more continuous and proactive process, identifying, measuring and managing risks across firm departments (Al-Rimawi, 2001).

The significance of risk management has been gradually increasing over the years and has showed exponential heights following the new Basel Capital Accord, the US Sarbanes Oxley Act, the European Sarbanes Oxley (8th Company Law Directive, E-SOX), the Japanese Sarbanes Oxley (Financial Instruments and Exchange Law, J-SOX), the European Union's financial Services Action Plan (FSAP) including MiFID (Markets in financial services directive, along with other Acts, Directives and Regulations).

The board of directors has specific responsibilities pertaining to risk management, which is defined through best practices, guidelines, laws and regulations (Bates & Leclerc, 2009). It is also the responsibility of the risk committee to help the board in assessing various kinds of risks that the organisation is vulnerable to. It is management's responsibility to execute the risk management policy of the organisation.

Additionally, an oversight role should be exercised by the executive committee and evidence to that effect should be provided. The committee members should have a direct access to management's regular reports. The committee must comprise of at least three members with the majority of the members being non-executive directors and one being a member of the audit committee. Moreover, at least one of the committee members must be a risk expert and the chairman of the committee must be a non-executive director (Omani Code of Corporate Governance, 2002).

Consistent with Al-Matari *et al.* (2012) and Yatim's (2010), this factor should be taken into consideration. The executive committee is one of the essential factors of internal corporate governance with other committees like the audit committee and ownership structure. The integrations between these committees help to improve and enhance firm's performance. In general, the literature is insufficient regarding the executive committee and its effect on the performance.

4.3.4.1 The Executive Committee Existence and Firm Performance

The literature regarding the relationship between executive committee's existence and firm performance is very limited. Thus, the executive committee is measured by the dummy variable, which means that if the company has this committee give it (1) if other gives it (zero).

In view of the agency theory, the large number of members on the board is expected to reduce the effectiveness of the committee since they spend more time to make a decision. The big size of the board or committee spread the perspective of members (Jensen & Meckling, 1976). In the same context, AbdurRouf (2011) and Yermack (1996) claimed that issues of coordination, communication and decision-making hinder the performance of the company upon increasing the number of directors. Therefore, with the inclusion of an extra member to the board, elements of diversity offset that of coordination. Moreover, Berle and Means (1932) and Fama and Jensen (1983) expound that external boards could reinforce the firm's value by bringing experience to the board and by their monitoring services. Along the same line, external directors have a role in safeguarding the interests of the shareholders through monitoring with their expertise, developed from their past experiences (Mace, 1986).

From the resource dependence theory's point of view, the board is responsible to obtain firm resources on the basis of the board members' relationship with other firms (Pfeffer, 1972; Provan, 1980; Zald, 1967). The theory further suggests that the larger the size of

the board, the better is the corporate governance, as the board becomes a pool of various skills, knowledge and expertise. Large boards are more capable to offer the diversity that would assist firms in securing critical resources and minimising environmental uncertainties (Goodstein *et al.*, 1994; Ghazali, 2010; Pearce & Zahra, 1992; Pfeffer, 1987). The extra members on the board help the committee through their experience and knowledge to bring about a superior decision, which in turn contributes to the enhancement of the firm's performance.

According to the resource dependence theory, the integration of the board independence depends on the board's contribution to improve performance of a firm. They can use their experience and knowledge to make a right decision at the right time (Pearce & Zahra, 1992; Pfeffer, 1987).

Due to the lack of literature, related to the relationship between the executive committee and firm performance and in the light of the agency theory and resource dependence theory, the following hypotheses are formulated:

H₁₁: There is a relationship between the executive committee existence and firm performance.

H_{11a}: There is a relationship between the executive committee existence and ROA.

H_{11b}: There is a relationship between the executive committee's existence and Tobin-Q.

4.4 Control Variables

In the literature, some variables such as firm size, debt, industry and year have been studied as control variables. Previous studies by Chiang and Lin (2011), Garcí'a-Meca and Sa'nchez-Ballesta (2011), Herly and Sisnuhadi (2011), Kang and Kim (2011), Karaca and Ekşi (2012), Khan and Javid (2011), Liang *et al.* (2011), Chaghadari (2011), Najid and Abdul Rahman (2011), Nuryanah and Islam (2011), Saibaba and Ansari (2011), Shan and McIver (2011) and Zureigat (2011) have tested the firm size and debt as control variables with firm performance when examining the determinants of firm performance. Moreover, this study is similar to prior studies that test the industry with firm performance such as, Bozec (2005), Cho and Kim (2007), Filatotchev, Isachenkova, And Mickiewicz (2007). Garg (2007) and Mandacı and Gumus (2010). They argued that the firm size, debt, industry and years affect firm performance. Therefore, this study, considers the firm size, debt, industry and years as the chosen control variables.

4.4.1 Firm Size

The use of firm size as the control variable is justified by the findings of companies with various distinct characteristics. According to Patro, Lehn and Zhao (2003), the possibility of firm size and growth are crucial determinants of the boards' size and structure. They revealed that the size of the firm is linked to the board size in a direct way and is inversely proportional to the growth opportunities proxy. They also found that

representation is inversely proportional to the size of the firm and linked to the proxy of opportunities for growth in a direct way. Hence, firm size impacts firm performance.

The size of the firm impacts firm performance and it is commonly utilised as a control variable in the empirical literature concerning corporate governance (e.g. Andres *et al.*, 2005; Ghosh, 2006). The impact of firm size upon corporate governance is evident in the findings, which illustrate larger companies to be less effective compared to smaller companies because although they meet government bureaucracy, they have more ambiguity and higher agency issues (Patro *et al.*, 2003).

Nevertheless, their use of economies of scale and employment of higher skilled management, make large firms more effective compared to their smaller counterparts (Kyereboah-Coleman & Biekpe, 2006). Along a similar line, Coles and Jarrell (2001) claimed that during the growth of the firm, it requires more board members who are specialised in monitoring it. According to the contention above, in Haniff and Hudaib's (2006) study, the natural algorithm of sales (LNSA) was used to measure the size while in Peng, Li, Xie and Su (2010), natural logarithm of the company's assets measured the size. The latter size measure is adopted in the present study.

4.4.2 Leverage

Leverage is a widely utilised control variable by several empirical studies examining the corporate governance-financial performance relationship (Chiang & Lin, 2011; Herly & Sisnuhadi, 2011; Kang & Kim, 2011; Karaca and Ekşi, 2012; Khatab *et al.*, 2011;

Kyereboah-Coleman & Biekpe; 2006; Chaghadari, 2011; Najid & Abdul Rahman, 2011; Wahla *et al.*, 2012). Such studies showed that debt impacts the financial performance of the firm. Firm leverage was measured by Alsaeed (2006) by dividing the total liabilities by total assets.

Debt ratio is described as the total sum of long-term debt and short-term/extended liability as a percentage of total assets. Debt ratio affects the company's outcomes. A positive impact may lead to minimised cash flow and control of the company to reveal more of the market.

Based on the agency theory, Jensen and Meckling (1976) claimed that the firm should have the leverage to reinforce its monitoring costs like increase in debt levels. Effective boards and committees are able to oversee management. The agency theory predicts that the level of leverage increase leads to a corresponding increase in board effectiveness. On the contrary, a negative impact of debt can stem from the failure or the cost of agency fees of debt (Jensen, 1993). The present study measures leverage by total liabilities divided by total assets.

4.4.3 Industry

Literature, dedicated to the industrial organisation holds the industry structure as a central determinant of corporate governance and firm performance (Porter, 1985). Several empirical researches evidenced the significance of industry factors. For instance, Zeckhauser and Pound (1990) revealed that in the context of industries with low asset

specificity, such as machinery and paper products, concentrated ownership results in higher performance, but in the context of industries with high specificity like computers, such effect is absent. In other words, the effectiveness of large holders in mitigating agency problems may hinge on the industry type.

In the same line of study, the performance outcomes are also influenced by industry in such a way that the relationships are significantly mediated by the debt levels susceptible to the sectors (Tarn & Tan, 2007). In the context of Taiwan, Chen (2006) showed that large block-holders are not in control of Taiwanese firms in high-tech industries and such firms have significantly greater firm values compared to other industries regardless of the types of large-block ownership they possess. Also in this line of study, Coles, McWilliams and Sen (2001) revealed that industry is a significant performance driver in the context of their sample firms, while Schmalensee (1985) demonstrated that industry constitutes around 19% of the differences in accounting rate of return. Wernerfelt and Montgomery (1988) extended Schmalensee's (1985) study by not using the accounting rate of return as they are distorted by their oversight of the differences in risk and tax laws – they instead employed a market to book ratio. Their findings were consistent with those of Schmalensee's in that industry effects are the main determinants of the success of firms. Moreover, according to Li and Simerly (1998), factors such as environmental dynamism may also differ industry-wise with the dynamic competition and maturity of the industry.

4.4.4 Time Period

This study utilises year as control variable in order to measure the performance of companies during the past five years. The use of this variable gives a clear indication about the performance of the companies over five years in order to know the reasons which led to the fluctuation of the performance of companies. Moreover, international markets experienced radical economic instability from 2008 to 2012 and relevant factors impacted the Omani firm's performance.

Furthermore, the two major measures, namely markets based and accounting based measures are individually distinct. While one looks forward (market-value) the other looks backward (accounting-based). Stated clearly, market-based refers to the estimation of what management will accomplish, whereas accounting-based refers to the estimation of what management has accomplished. In this regard, Bhagat and Black (2002) revealed that stock price returns are vulnerable to the investor's expectations. In addition, market value is different from accounting value based on who is measuring performance. In the former, performance is determined by the investors with curtailed by their acumen, optimism or pessimism while in the latter, it is determined by the accountant curtailed by professional standard and market value. Because economists are more privy to market constraints as opposed to accounting constraints, majority of empirical studies employs market value like Tobin's-Q. Nevertheless, accounting rate may be superior as it is not influenced by the investors' psychology.

4.5 Summary of the Chapter

This chapter explains the research methodology and provides the formulated hypotheses. It also provides an explanation of the theoretical framework based on the agency theory and resource dependence theory. Finally, it discusses the formulation of hypotheses and the control variables.

CHAPTER FIVE

RESEARCH METHODOLOGY

5.1 Introduction

This chapter presents the research methodology of the study, which will help in the next steps of investigation and analysis. The chapter highlights the research process beginning with the research design comprising of data collection, panel data, data collection procedures, unit of analysis, specification of the model and multivariate regression along with the variables' measurement. The chapter also explicates the proposed panel data analysis technique, data analysis and interpretation.

5.2 Research Design

In order to achieve the objectives of study, the correlational studies are utilised to investigate the relationship between CG elements such as board of directors' characteristics (board size, board independence, board meeting, board change, secretary role, legal counsel and foreign member on the board), audit committee characteristics (size, independence and meeting), executive committee as independent variables and firm performance (ROA and Tobin-Q) as dependent variables.

5.3 Panel data

In the present study, panel data method is utilised to investigate the impact of the independent variables on the dependent one, namely accounting conservatism. This method has been employed in prior studies in the field of accounting. In the same line, this study uses panel data form 2008 to 2012. For instance, in studies conducted by Azam, Usmani and Abassi (2011), Banker, Devaraj, Schroeder and Sinha (2002), Bhattacharya *et al.* (2003), Fazlzadeh, Hendi and Mahboubi (2011), Gurbuz and Aybars (2010), Ibrahim and Abdul Samad (2011), Heenetigala and Armstrong (2011), Herly and Sisnuhadi (2011), Karaca and Ekşi (2012), Leng (2008), Liang, Lin and Huang (2011), Ming and Gee (2008), Rustom, Rashid, Zaman (2013), Sanchez-Ballesta and Garcia-Meca (2007), Schiehl (2006) and Swamy (2011). In addition, STATA statistical software version 12 is utilised for data analysis as it is appropriate for panel data regression.

Panel data is also called longitudinal data or cross sectional time series data and it is described as data on the same observed subjects over a period of time. According to Greene (2008), some issues cannot be examined with the help of cross-sectional or time series data; for instance, the conservative accounting of firms can be suitably examined if such firms are observed over some period of time (Ahmed & Duellman, 2007; Roychowdhury & Watts, 2007). Accordingly, the present study has investigated 78 firms during a 5-year period.

Panel data has been invaluable in the field of social sciences, as it has enabled researchers to conduct longitudinal analysis in various fields. By repeatedly observing cross-sections, panel data allows the researcher to examine the change dynamics with the help of short time series. In fact, the combined methods of time series and cross-sections can improve data quality and quantity in a manner that would not be possible when using any of the two singularly (Baltagi & Wu, 1999; Greene, 2003; Gujarati, 2003).

Analysis of panel data provides regression analysis with a spatial as well as temporal dimension. Thus, it becomes possible to control some omitted variables, although instead of observing them, the dependent variable changes are observed for a period of time. This controls different omitted variables by case, but similar over time. Panel data may also be used to control omitted variables that differ over a period but are constant case wise. Several kinds of panel data analytic models exist, including constant coefficient models, fixed effects models and random effects models.

Panel data reveals that subjects comprising of countries, states, firms or individuals, are heterogeneous in nature, indicating that despite the variation of some variables throughout subject and time, there are other variables that may be invariant either by time or by subject. Those that are subject invariant comprise of factors that impact the entire subjects, but differs across time while those that are time invariant comprise of factors that are constant in terms of time and they are distinct subjects. These variables should be included in the model equation in order to steer clear of bias in the resulting estimates. Furthermore, panel data method enables the control of these invariant factors that are left

uncontrolled in cross sectional and time series studies. Another justification for the use of panel data is its solution to the omitted variable issue (Wooldridge, 2002, p. 247).

Panel data provides benefits over pure cross sectional and pure time series analysis as provided by Hsio (2003) and Baltagi (2008). Firstly, panel data offers a more robust information source as it considers multiple observations on cross sectional units. Hence, it furnishes ample variability and is a more accurate estimation of parameters. The informative data also offers accurate estimates and tests a complex behavioural model having little to no confining assumptions. Secondly, in case of pure time series data, the serious issue of multicollinearity arises among the independent variables (X), in that the current period independent variables (X_t) are highly correlated with those of the prior period (X_{t-1}). Thus, for panel data, X differences throughout cross sectional units can be employed to mitigate collinearity because the grouping of cross sectional and time series data adds to the variability that can be disintegrated into between subjects-variation and within subjects-variation. Thirdly, panel data controls individual heterogeneity by resolving or decreasing the issue of omitted variables stemming from the erroneous measurement or no observed items correlating with the model's independent variables. Fourthly, panel data enables the examination of complex issues of dynamic behaviours as it identifies and estimates the impacts that are non-detectable in cases of pure cross section or time series data. Finally, panel data allows the identification of unidentified model, which normally may be undetectable owing to errors in measurement.

5.4 Data Collection Procedures

As discussed earlier, the required data for the study concerning CG and firm performance is gathered from annual reports of the companies listed in the Omani trading stock market website, the Muscat Securities Market (MSM) (<http://www.msm.gov.om/>). More specifically, the data regarding the corporate governance are collected from the part explaining the corporate information and the CG statements and from the profile of the director. The data regarding the firm performance is collected from corporate statements such as balance sheet, income statement, and cash flow statement incorporated in the annual reports, while stock prices are gathered from Data stream.

5.4.1 Population and Sample

This study utilises panel data for five years from 2008 to 2012. Moreover, this study uses the panel data analysis for many reasons as discussed above. The MSM lists 123 firms, which all are categorised into groups according to their similarities. The study population consists of the category of non-financial firms listed in this MSM (<http://www.msm.gov.om/>). According to the above MSM, there are 87 non-financial companies included on the main board and secondary board as of 20th September 2012. This study has selected all the non-financial firms comprising of 78 (Available data) firms during 2008, 2009, 2010, 2011 and 2012. Therefore, total observations of this study are 390 data points.

Table 5.1
Sample of Study

Year	No. of the firms	Availability
2008	87	78
2009	87	78
2010	87	78
2011	87	78
2012	87	78
Total	435	390

Furthermore, it excludes financial firms (banks) because of their structure, methods and the accounting practices that differ substantially from non-financial firms (Barontini & Caprio, 2006; Bøhren & Strøm, 2010; Imam & Malik, 2007; Mandacı & Gumus, 2010; Maury, 2006; Schiehl & Bellavance, 2009; Wei, 2007) and the performance associated is not straight forward (Cyril & Sarimah, 2008).

Moreover, Mehran, Morrison and Shapiro (2011) claimed that there are two primary distinctions between banking sector governance and non-financial sectors. Firstly, banks possess a significant number of stakeholders compared to their non-financial counterparts. Secondly, banks are opaque, complex and dynamic in an expedient manner. The financial sector's complexity, specifically the banking sector, leads to challenges of the formal regulations implementation. Owing to the regulatory differences between financial and non-financial firms, the present study confines the focus on financial firms. Hence, information for the 78 non-financial firms are gathered and used for the purpose of testing the hypotheses. Because data is collected for five years, the total data points used equals data gathered from 390 firms.

The objective of this study is to examine the influence of CG mechanisms such as board of directors' characteristics (board size, board independence, board meeting, board change, secretary role, legal counsel and foreign member on the board), audit committee characteristics (size, independence and meeting) and executive committee on firm performance (ROA and Tobin-Q).

5.4.2 Instruments

In total, the data of the current study has been obtained from two different sources. Firstly of all, the data for board of directors' characteristics (board size, board independence, board meeting, board change, secretary role, legal counsel and foreign member on the board), audit committee characteristics (size, independence and meeting), executive committee, the control variables (firm size, leverage and the industry) and ROA have obtained from the annual reports of firms from the MSM website (2012). Secondly, data for companies share prices to compute Tobin-Q has taken from the Data Stream.

This study has used two proxies to measure firm performance, such as ROA: Earnings before tax divided by total assets of the company. Additionally, Tobin-Q Ratio (TOBINSQ): The market value of equity plus the book value of the debt divided by the book value of the total assets.

Furthermore, this study uses many variables to measure CG, board size has been defined by Al Manaseer *et al.* (2012), Nanka-Bruce (2011), O'Connell and Cramer (2010) and Rachdi and Ameer (2011) to be the number of directors on the board. Board

independence can be defined as the number of independent non-executive members positioned in the board relative to the total number of members (Lawal, 2012; Uadiale, 2010). Moreover, the board meeting represents the number of meetings the board has during a year (Al Manaseer *et al.*, 2012; Kang & Kim, 2011; Li *et al.*, 2012; Nanka-Bruce, 2011; Obiyo & Lenee, 2011). Besides, the board change is defined as the appointment of a new member on the board during a year and is measured by using a dummy variable. Furthermore, the role of secretary on the board is crucial in the board and is measured by using a dummy variable. Likewise, the role of legal counsel on the board is crucial in the board and is measured by using a dummy variable. Finally, foreign member on the board can be measured by the number of non-executive foreign directors divided by the total number of board members.

Audit committee size is measured by the number of members serving on the audit committee of the firm (Bauer *et al.*, 2009; Hsu & Petchsakulwong 2010; Nuryanah & Islam, 2011; Obiyo & Lenee, 2011). Moreover, the audit committee independence is measured through the ratio of non-executive members of the committee (Abdullah *et al.*, 2008; Kang & Kim, 2011). An audit committee meeting can be measured by the frequency or number of meetings during a year for the audit committee (Hsu & Petchsakulwong, 2010; Khanchel, 2007; Kyereboah-Coleman, 2007; Rahmat, Iskandar & Saleh, 2009). The executive committee is measured by by using a dummy variable. Meaning that, if the company has a committee give (1) if other gives (zero).

Finally, it has used many variables to measure, control variables such as firm size, which can be measured by the natural log of total assets. Moreover, leverage can be measured by the ratio of total liabilities to total assets. Industry can also be measured by dummy variable which means that, if the firm is an industry give (1) if other gives (zero). Moreover, time period can also be measured by a dummy variable which means that value of one for the specific year and zero otherwise.

5.5 Unit of Analysis

This study aims to investigate the hypothesis relationship in corporate unit level; therefore, the unit of analysis in this study is the organisational level represented by each company in the Omani Public Listed Boards.

5.6 Model Specification and Multivariate Regressions

The multivariate regression analysis is utilised to investigate the relationship between firm performance listed on the MSM and the determinants of CG.

The multivariate regression analysis result is an equation representing the most accurate prediction of the dependent variable on the basis of the independent variables. This method is utilised in cases where the independent variables are interrelated with one another and with the dependent variable.

The regression equation is depicted as follows:

Model1:

$$\text{ROA} = \alpha_0 + \beta_1 * \text{BOARDSIZE} + \beta_2 * \text{BORADINDE} + \beta_3 * \text{BOARDME} + \beta_4 * \text{BOARDCH} + \beta_5 * \text{SECRETATA} + \beta_6 * \text{LEGALCO} + \beta_7 * \text{BOFOREIGN} + \beta_8 * \text{ACSIZE} + \beta_9 * \text{ACINDE} + \beta_{10} * \text{ACMEETIN} + \beta_{11} * \text{ECEX} + \beta_{12} * \text{FIRMSIZE} + \beta_{13} * \text{LEVERAG} + \beta_{14} * \text{INDUSTRY} + \beta_{15} * \text{TIMEPER} + \varepsilon \quad (1)$$

Model 2:

$$\text{TOBINSQ} = \alpha_0 + \gamma_1 * \text{BOARDSIZE} + \gamma_2 * \text{BORADINDE} + \gamma_3 * \text{BOARDME} + \gamma_4 * \text{BOARDCH} + \gamma_5 * \text{SECRETATA} + \gamma_6 * \text{LEGALCO} + \gamma_7 * \text{BOFOREIGN} + \gamma_8 * \text{ACSIZE} + \gamma_9 * \text{ACINDE} + \gamma_{10} * \text{ACMEETIN} + \gamma_{11} * \text{ECEX} + \gamma_{12} * \text{FIRMSIZE} + \gamma_{13} * \text{LEVERAG} + \gamma_{14} * \text{INDUSTRY} + \gamma_{15} * \text{TIMEPER} + \varepsilon \quad (2)$$

Where:

α_0 – Constant

ROA: Return on Assets- earnings before tax divided by total assets of the company.

TOBINSQ: Tobin-Q Ratio- the market value of equity plus the book value of the debt divided by the book value of the total assets.

BOARDSIZE: The Board Size- the total number of directors serving on the board of directors.

BORADINDE: The Board Independence- the number of independent non-executive directors on the board relative to the total number of directors.

BOARDME: The Board Meeting- the frequency number of meetings during a year for the board directors.

BOARDCH: The Board Changes- dummy variable 1 if the board has a new appointment during a year and 0 others.

SECRETARY: The Secretary Role on the Board- dummy variable 1 if the board has a secretary and 0 others.

LEGALCO: The Legal Counsel- dummy variable 1 if the firm has the legal counsel and 0 others.

BOFOREIGN: The Foreign Member on the Board- the number of non-executive foreign directors divided by the total number of board members.

ACSIZE: The Audit Committee Size- the number of members serving on the audit committee.

ACINDE: The Audit Committee Independence- the number of non-executive members serving on the audit committee.

ACMEETIN: The Audit Committee Meeting- the frequency number of meetings during a year for the audit committee.

ECEX: Executive Committee Existence- dummy variable 1 if the firm has a executive committee and 0 others.

FIRMSIZE: Firm Size- the natural log of total assets.

LEVERAG: Leverage- the ratio of total liabilities to total assets.

INDUSTRY: Industry- dummy variable 1 if the firm is industry and 0 others.

TIMEPER: the Time Period- dummy variable whose value is 1 during the period and 0 otherwise.

ε : Error term

In order to examine the relationship between the set of predictors and the dependent variable, the dependent variables are all keyed into the regression equation in a simultaneous manner. The results of the regression analysis can determine how each independent variable can contribute in explaining the variance in the firm performance.

5.7 Measurement of the Variables

The present section discusses the measurements of dependent variables, independent variables, moderating variables and control variables. The measurements of the variables of the study are elaborated as follows:

Table 5.2

Summary of Variables Measurement

N0.	VARIABLES	ACRONYM	OPERATIONALISATION	SOURCE
Dependent Variables (DV)				
1	Return On Assets ratio (%)	ROA	Earnings before tax divided by total assets of the company.	(Ali & Nasir, 2014; Al-Matari <i>et al.</i> , 2012; Al-Matari <i>et al.</i> , 2012a; Kaur, 2014; Müller, 2014; Saibaba & Ansari, 2013).
2	Tobin-Q Ratio (%)	TOBINSQ	The market value of equity plus the book value of the debt divided by the book value of the total assets.	(Al-Matari <i>et al.</i> , 2012a; Al-Matari <i>et al.</i> , 2012b; Jermias & Gani, 2014; Kamardin, 2009; Vo & Nguyen, 2014).
Independent Variables (IV)				
3	Board Size (number)	BOARDSIZE	Total number of directors serving on the board of directors.	(Danoshana & Ravivathani, 2014; Liang, Xu, & Jiraporn, 2013).
4	Board Independence (%)	BORADIN	The number of independent non-executive directors on the board relative to the total number of directors.	(Al-Najjar, 2014; Jermias & Gani, 2014; Liang, Xu, & Jiraporn, 2013; Müller, 2014).

Table 5.2 (Continued)

N0.	VARIABLES	ACRONYM	OPERATIONALISATION	SOURCE
5	Board Meeting (number)	BOARDME	The frequency number of meetings during a year for the board directors.	(Danoshana & Ravivathani, 2014; Liang, Xu, & Jiraporn, 2013; Sahu & Manna, 2013)
6	Board Change	BOARDCH	Dummy variable 1 if the board has a new appointment during a year and 0 others.	(Fox & Opong, 1999).
7	The Secretary on the Board	SECRETA	Dummy variable 1 if the board has a secretary and 0 others.	
8	The Legal Counsel	LEGALCO	Dummy variable 1 if the firm has the legal counsel and 0 others.	
9	The Foreign Member on the Board (number)	BO_FORE	The number of non-executive foreign directors divided by the total number of board members.	(Miletkov <i>et al.</i> , 2011; Ruigrok <i>et al.</i> , 2007).
10	Audit Committee Size (number)	ACSIZE	Number of members serving on the audit committee.	(Al-Matari <i>et al.</i> , 2012; Danoshana & Ravivathani, 2014; Ghabayen, 2012).
11	Audit Committee Independence (%)	ACINDE	Number of non-executive members serving on the audit committee.	(Al-Matari <i>et al.</i> , 2012a; Al-Matari <i>et al.</i> , 2012b; Chechet, Jnr & Akanet, 2013; Ghabayen, 2012).

Table 5.2 (Continued)

N0.	VARIABLES	ACRONYM	OPERATIONALISATION	SOURCE
12	Audit Committee Meeting (number)	ACMEETIN	The frequency number of meetings during a year for the audit committee.	(Al-Matari <i>et al.</i> , 2012b; Chechet, Jnr & Akanet, 2013; Saibaba & Ansari, 2013).
13	The Executive Committee Existence	ECEX	Dummy variable 1 if the firm has a executive committee and 0 others.	
Control Variables (CV)				
14	Firm Size (number)	FIRMSIZE	The natural log of total assets.	(Haniff & Huduib, 2006; Peng, Li, Xie & Su, 2010).
15	Leverage (%)	LEVERAG	The ratio of total liabilities to total assets.	(Karaca and Ekşi, 2012; Khatab <i>et al.</i> , 2011; Najid & Abdul Rahman, 2011; Wahla <i>et al.</i> , 2012).
16	Industry	INDUSTRY	Dummy variable 1 if the firm is industry and 0 others.	(Chen, 2006; Tarn & Tan, 2007).
17	Time period	TIMEPER	Dummy variable whose value is 1 during the period and 0 otherwise.	(Gupta & Sharma, 2014).

5.8 Proposed Panel Data Analysis Technique

The collected data has been analysed with the use of STATA version for describing the data and testing the hypothesised relationships.

5.8.1 Descriptive Analysis

The descriptive analysis reported the mean, minimum, maximum and the standard deviation of every variable.

5.8.2 Correlation of Variables

The interrelationship between the variables has been examined through the use of the correlation analysis. The results of the analysis indicate the correlation, nature, direction and significance of the relevant variables correlation.

5.8.3 Diagnostic Tests

The diagnostic tests that were employed on the data are explained in the present section. Firstly, the diagnostic tests were employed in the distribution of data in light of normality, extreme outliers, and multicollinearity. This was followed by the diagnostic tests employed, particularly for the panel data, including normality, outliers, multicollineari, contemporaneous correlation, heteroskedasticity and autocorrelation.

5.8.3.1 Normality

Normality is described as the shape of the distribution of data for individual quantitative data variable and its normal distribution. It is a basic assumption in multivariate analysis that follows the premise that a significant deviation from normality will result in an invalid statistical outcome (Hair, Black, Babin, Anderson and Tatham, 2006). The residual, in multivariate analysis, is the difference between the values (observed and predicted) and is expected to possess independent and normal distribution. As such, the researcher assessed the residual for normality testing. In case the residuals meet the assumption, the normality of individual variables should be checked (Tabachnick & Fidell, 2007). Among the common statistical normality tests are skewness and kurtosis. The former refers to the distribution balance, where an abnormally distributed skewness shifts to the left or the right side. The latter on the other hand, refers to the distribution peakedness or flatness in relation to normal distribution. Kurtosis and skewness usage in statistical tests are sensitive to a large set of data (Tabachnick & Fidell, 2007). A variable characterised by skewness or kurtosis does often display considerable deviation from normality and hence, does not significantly impact the analysis. According to Tabachnick and Fidell (2007), the distribution shape can be observed on a graph. The residual distributions according to standardised normal probability plots (*pnorm*) that are sensitive to non-normality in the middle data range were noted.

5.8.3.2 Outliers

A normality problem stemming from outliers can be solved through transformation, although several researchers do not advocate it. Specifically, Grissom (2000) contended that the transformed data can often cause the reverse of the mean difference of the actual data. Along the same line of contention, Tabachnick and Fidell (2007) emphasise that transformations of data are not recommended, although they may be effective for outliers and normality failures. In the present study, multivariate outliers were detected Mahalanobis distance measure as suggested by Hair *et al.* (2010). The researcher further investigated extreme points highlighted to guarantee that they did not stem from error in data entry.

5.8.3.3 Multicollinearity

Notable researchers (Tabachnick and Fidell, 2007 and Hair *et al.*, 2010) stated that an issue of multicollinearity arises if the independent variables correlation goes over 0.9. Along with the correlation test, the variance inflation factor (VIF) was conducted because the examination of the matrix correlations between variables does not always detect multicollinearity (Hamilton, 2009). VIF indicates the impact that other independent variables have on the standard error of regression coefficients. Collinearity problems are said to exist if VIF is over 10.

5.8.3.4 Contemporaneous Correlation

Contemporaneous correlation, also referred to as cross-sectional dependence, is the correlation of unobserved factors throughout the units. This correlation has a tendency to rise in a sample having cross-section units (Wooldridge, 2003). The significant interdependencies among cross-sectional units can stem from the economic and financial factors included in state and financial entities. Hence, an identical reaction may be experienced by individuals according to their interdependent preferences, neighbourhood effects, herd behaviour and social norms. Oversight of the presence of this correlation may lead to standard error estimation bias.

STATA was employed to test cross-sectional dependence with the help of *xtcds*, *pesaran* syntax, which is applicable for large N and small T panel data (Hoyos & Sarafidis, 2006). This process involves the application of a parametric testing procedure recommended by Pesaran (2004).

5.8.3.5 Heteroskedasticity

Homoskedasticity is described as the condition where the error process is distributed in an independent and identical manner. In this regard, despite the fact that the error process may be homoskedastic throughout cross-sectional units, it may have different variance across units in a condition known as group wise heteroskedasticity (Baum, 2001). Baltagi (2008) stated that the assumption that homoskedasticity in regression disturbance within

a panel data model was a restrictive one as each unit possesses its constant individual features or heterogeneity.

Baltagi (2008) added that the oversight of the existence of the generated heteroskedasticity leads to a consistent but inefficient estimation of the regression coefficients coupled with biased error estimates. The error term heteroskedasticity is examined on the basis of a modified Wald Statistic as recommended by Baltagi (2008). The detection of heteroskedasticity issue can be solved through White's Heteroskedasticity Consistent Variance and Standard Error method, Weighted Least Square method or by data transformation as recommended by researchers (e.g. Hair *et al.*, 2006; Gujarati, 2003; and Cheng *et al.*, 2001).

5.8.3.6 Autocorrelation

Autocorrelation or serial correlation is the correlation between error components over a period of time. This goes against the classical assumption of regression analysis, but often arises as error term characteristic in the context of time series analysis (Wooldridge, 2003). According to Green (2008, 211), autocorrelation has a tendency to influence the estimated covariance matrix of the least square estimator more than heteroskedasticity. The autocorrelation detection test was conducted with the help of *xtserial* syntax, STATA that employs a test of serial correlation of a linear panel-data model's idiosyncratic errors (as explained by Woodridge, 2002).

The existence of autocorrelation can also be determined through the use of the Durbin-Watson test. The presentation of regression results for time series data entails the result for the Durbin-Watson test for autocorrelation where a d closer to zero indicates positive correlation, while that's closer to 4 indicates negative correlation. The model is said to have either positive or negative correlation by determining the required proximity to the above values, where there are upper and lower critical values for d . These values depend on the number of observations (N) as well as the number of explanatory variables (k).

5.9 Data Analysis and Interpretation

Prior to the analysis, data should be made ready through cleaning and screening after which diagnostic tests are conducted and panel data method is employed to the models.

5.9.1 Getting Data Analysis-Ready

Data cleaning and screening before the actual analysis takes a significant amount of time and it can be a tedious task. However, it should be kept in mind that issues should be resolved prior to the testing of the main analysis to guarantee accurate data analysis (Tabachnick & Fidell, 2007). After entering the entire data into the worksheet, incomplete data is not included. The statistical package for social science (SPSS), version 21 and STATA, version 12 were used in testing and processing data. Prior to hypotheses testing, there are certain steps that have to be run in order to make sure that data is of good quality. Sekaran (2003) described these steps as data cleaning and screening.

5.9.2 Panel Data Analysis

The simple OLS regression considers sample companies to be homogeneous and thus, it ignored heterogeneity in contrast to the panel regression method. In this regard, panel data that is analysed with the help of the OLS regression method was examined by Jager (2008) according to its comparison or contrasting results from those analysed with the help of panel data method. The results revealed that the methods significantly differ and this indicates that using the OLS method on panel data would result to erroneous assumptions.

Observations in panel data cannot be considered to be independently distributed throughout time owing to the unique individual characteristics that remain constant for a period of time (Baddeley & Barrowclough, 2009; Wooldridge, 2003). In other words, if pooled OLS employed in cross-sectional or time series analysis, displaying homogeneity, is gauged through panel data, may result in erroneous assumptions (Baddeley & Barrowclough, 2009). On the other hand, simple pooling through penal data entails no modification for firm specific-factors, which leads to autocorrelation due to the fact that for every year, the distinct factors of the firm is deemed as residuals. In addition, it also leads to heterogeneity bias in light of deleted variables bias because the distinct firm features are not included in the deterministic portion of the model (Baddeley & Barrowclough, 2009). Panel data heterogeneity effect employs a fixed effects model or random effects model. The primary distinction between the two methods is if the error term is associated with independent variables.

5.9.2.1 Fixed Effects Model

Every entity's attributes are unique to itself and they remain constant throughout time. These attributes may or may not impact dependent variables. The fixed effects model examines the dependent-independent variable's relationship and maintains their time-invariant factor that may impact the former variables. Based on the premise that underlies the utilisation of fixed effects method stating that there is a correlation between error term and independent variables, the method deletes the impact of unobserved time-invariant features from the independent variables in an attempt to assess such variables net effect. This indicates the unbiased nature of this method as it maintains unobserved time variant factors, although it may prove inefficient if the assumed correlation actually has zero values (Allison, 2009).

The implementation of the fixed effects method is possible through dummy variables or mean deviation technique. The former creates a set of dummy variables for every entity within the set of data. Moreover, the coefficient of the dummy variables in the entity, generated during the analysis, reflects an estimation of the unobserved time-invariant factors.

Despite its benefits, the fixed effects method according to Wooldridge (2003) is impractical for data sets characterised by several cross sectional observations. Additionally, it may function beyond the accounting software capacity (Allison, 2009). On the other hand, the mean deviation method is another method that can be used instead

of estimated fixed effects regression, with the former entailing the mere simple use of accounting software. This indicates that the mean values for the entire time-varying variables are determined for every entity. The entity's specific means are subtracted from each variable's observed value. As for the time-invariant independent variables' estimate coefficients, they are not provided as they have constant values for each entity. Thus, when the time-invariant variables' entity-specific mean is subtracted from the individual values, a value of zero remains. As such, the time-invariant independent variables are deleted from the equation to control their effect (Allison, 2009).

5.9.2.2 Random Effects Model

The random effect model is advantageous over the fixed effects model in that, independent variables that are time constant can be studied with the help of a regression model. Nevertheless, if it goes against the premise that there is no correlation of the fixed effects with disturbances displayed within effects, a biased outcome may be reached. In the final step, the Hausman test was employed for the comparison between fixed effects and random effects with the underlying basic question of the test as whether or not a significant correlation exists between the individual effects and the regressors. The lack of such correlation would advocate in favour of the fixed effects model as the random effects model generates biased estimators.

5.10 Multivariate Regression Analysis

As discussed earlier, to test proposed model this study employed the multivariate regression using Panel data (STATA version 12) and IBM SPSS (version 21).

5.11 Summary of the Chapter

This chapter summarises the research design and the meteorological aspect of this study. It also reports the operational definitions of the variables used. In addition, the model discussed in this study is developed and the proposed analysis techniques are briefed.

CHAPTER SIX

ANALYSIS AND FINDING

6.1 Introduction

The subsequent chapter presents the findings and the data analysis results associated with the developed model of this study. Specifically, this chapter is divided into ten major sections as follows; Section 6.2 presents the Analysis of the Sample. While Section 6.3 presents the companies' profile and Section 6.4 provides the descriptive statistics of the variables used in the regression tests. The correlation analysis is presented in Section 6.5 and Section 6.6 reports the results of panel data. The LM test is discussed in Section 6.7 while Section 6.8 reports the F test. GLS estimates are presented in Section 6.10.

Additionally, the model estimation is reported in Section 6.11. Section 6.12 presents an evaluation of the models. Furthermore, the summary of hypotheses testing of the basic model is discussed in Section 6.13. Moreover, Section 6.14 offers the summary of hypotheses testing of corporate governance and firm performance. Further, models' equation is presented in Section 6.15. Finally, Section 6.16 ends with the concluding remarks of the chapter.

6.2 Analysis of the Sample

The study sample comprised of listed MSM with the exclusion of financial ones at the end of 2008, 2009, 2010, 2011 and 2012. The number of listed companies in the MSM is

78 and the sample companies, excluding financial companies, in the list providing complete information about their CG attributes totalled 435 companies, but owing to the availability of data for the five years, only 390 companies were included in the sample.

The data on the relationship between the board of director's characteristics, audit committee characteristics, the executive committee and firm performance were collected through the annual reports of Oman public listed companies during 2008 to 2012. The company's name was needed to align the company's CG information with its financial information.

Table 6.1

Analysis of the Sample

Year	No. of the firms	Availability
2008	87	78
2009	87	78
2010	87	78
2011	87	78
2012	87	78
Total	435	390

6.3 Companies Profile

Table 6.2 shows the profile of the firms with regards to the board change variable. Based on the results, only 168 firms of the 390 firms have changed their board during a year, whereas 222 companies of the Omani firms did not change their board during the same

year. This indicates that the MSM companies employed a superior practice of CG, which revealed the appointment of capable individuals to enhance the firm's performance.

Table 6.2
Frequency of the Companies Regarding to the Board Change Variable

The Board Change	Frequency	Percentage
Board Change	168	43.1%
No change	222	56.9%
Total	390	100%

Table 6.3 shows the profile of the firms with regards to the secretary appointment. Based on the results, 256 out of 390 firms have secretaries of the board, whereas 134 companies of the Omani firms have no secretaries. This indicates that the companies listed in the Muscat Securities Market (MSM) employed the best practice of corporate governance and followed up good methods to maximise the company's performance in order to attract investors.

Table 6.3
Frequency of the Companies Regarding to the Secretary Variable

The Secretary	Frequency	Percentage
Secretary	256	65.6%
No secretary	134	34.4%
Total	390	100%

In the same line, Table 6.4 shows the profile of the firms with regards to the legal counsel variable. Based on the results, 242 out of 390 firms have legal counsel during the specific year, whereas 148 companies of the Omani firms have no legal counsel during the same year. This result also indicates that the companies employed a superior corporate governance practice and hired capable individuals armed with superior methods to increase company performance to attract investors.

Table 6.4
Frequency of the Companies Regarding to the Legal Counsel Variable

The Legal Counsel	Frequency	Percentage
Legal	242	62.1%
No legal	148	37.9%
Total	390	100%

Along the same line, Table 6.5 shows the profile of the firms in terms of the executive committee existence variable. Based on the results, 192 firms from 390 have executive committee. The finding shows that the majority of firms listed on the MSM has no established committees – in this regard, it is important that they do as they have to follow the best practice of CG in order to attract both local and foreign investors.

Table 6.5
Frequency of the Companies Regarding to Executive Committee Existence Variable

The Legal Counsel	Frequency	Percentage
ECX	192	49.2%
No ECX	198	50.8%
Total	390	100%

Likewise, Table 6.6 shows the profile of the firms regarding industry variable. Based on the results, 240 of 390 firms are industry companies and 150 of 390 are non-industry firms. This finding indicates that the MSM applies a superior policy in sector distribution because this will encourage both types of investors to invest in the companies.

Table 6.6
Frequency of the Companies Regarding to Industry Variable

The Legal Counsel	Frequency	Percentage
Industry	240	61.5%
No Industry	150	38.5%
Total	390	100%

6.4 Descriptive Statistics

Table 6.7
Descriptive Statistics of Continuous Variables

Variable	Unit	Mean	Std. Dev.	Min	Max
Board Size (BOARDSIZE)	Number	7.072	1.407	5.000	12.000
Board independence (BORADINDE)	Ratio	0.876	0.195	0.000	1.000
Board Meeting (BOARDME)	Number	5.762	1.848	0.000	15.000
Foreign Member (BOFOREIGN)	Ratio	0.258	0.255	0.000	1.000
Audit Committee Size (ACSIZE)	Number	3.510	0.720	2.000	7.000
Audit Committee Independence (ACINDE)	Ratio	0.932	0.183	0.000	1.000
Audit Committee Meeting (ACMEETIN)	Number	4.849	1.295	0.000	10.000
FIRM SIZE (FIRMSIZE)	OR	49181392	103501646.7	605320	685377000
LEVERAGE (LEVERAG)	Ratio	0.483	0.272	0.024	1.721
Return On Assets (ROA)	Ratio	0.072	0.139	-0.487	1.631
Tobin-Q Ratio (TOBINSQ)	Ratio	1.297	0.571	0.273	3.928

Table 6.7 illustrates the descriptive statistics of the continuous variables. The descriptive statistics include mean, standard deviation, minimum and maximum, which were computed using State version 12. Based on the descriptive analysis as summarised in Table 6.7, the mean value of the board size (BOARDSIZE) in the Omani companies is about seven (7) members with a minimum of five (5) members and a maximum of twelve (12) members. The board size of the sample companies in this study was not much different from the studies that were examined in the GCC. Aljifri and Moustafa (2007) in the United Arab Emirates (UAE) had eight (8), Al-Matari *et al.* (2012b) and Ghabayen (2012) in Saudi Arabia found eight (8) and Al-Matari *et al.* (2012) in Kuwait found six (6). This result shows that the number of board of directors in the companies listed on the MSM is in adherence to the CG code. The CG practice effectiveness is considered to be a board function where it has a key role in the company management and direction of managers (Farrar, 2005; Nuryanah & Islam, 2011). It also has a key monitoring role as, ownership and control of the company are two separate entities (Jensen & Meckling, 1976).

In Oman, large number of board members urges authorities to enumerate points that are directed to achieve the firm target and aims. These roles help firms to protect shareholder wealth. This also suggests that Omani stock market companies, on average, choose their number of board members just optimally. According to Lipton and Lorsch (1992), this is generally good for firm performance as the ideal number of board members should be seven or eight. Firstenberg and Malkiel (1994) also contended that a board with less than

eight members can maintain an accurate focus, participation and productive interaction and debate. This is also consistent with Shaver's (2005) statement, which read that larger boards often display responsibility diffusion, social loafing, group fractionalisation, and less strategic change commitment.

Regarding the board independence (BORADIN), the outcome in the Table 6.7 reveals that the mean value of the board independence is 88 % with a minimum of zero and a maximum of 1 (100) %, suggesting that the board of Omani Stock market companies comprised of a mix of executive and non-executive directors. This result is consistent with the regulations in Oman that requires companies to have majority external directors on the board. The majority of the board should be non-executive directors because board independence has a major monitoring role (Lin, 2011).

Global corporate practices indicate that independent members should be included in the board (Nuryanah & Islam, 2011). Along the same line, independent directors lessen the agency cost as they facilitate effective monitoring and strategic planning (Berle & Means, 1932).

In addition, Fama and Jensen (1983) contended that external directors possess reputations as well as status to protect and these function as monitoring management incentives and guarantees effective running of the company. Moreover, the independence of the board also helps in minimising the agency problem and accordingly, shareholders should

request for the replacement of internal directors with external for effective management monitoring (Hermalin & Weisbach, 1991; Weisbach, 1988).

Consistent with the resource dependence theory, the firm's external sources provide the firm with an external gateway for the purpose of improving company's performance. An independent board also enables board members to understand complex environments and provide various knowledge and experience from different sources, which in turn enhance the performance of the firm (Pfeffer, 1972). Stated differently, an independent board provides the company with many sources to assist it in taking effective decisions. The proportion of the non-executive directors (NEDs) in this study are quite high as compared to that in the studies carried out by Al-Matari *et al.* (2012) and Ghabayen (2012b) in Saudi Arabia, which is 57 % and 49 % respectively and Al-Matari *et al.* (2012) in Kuwait which is 74 per cent.

The result in Table 6.7 also indicates that the mean board meeting (BOARDME) is about six (6) times a year with a minimum of zero (0) and a maximum of fifteen (15) times. The Omani Code of Corporate Governance (2002) stipulates that the board shall have a meeting at least 4 times a year with a maximum of 4 month gap between two meetings. The frequency of board meetings is a good indication of board effectiveness. This can lead to the enhancement of the firm performance as frequent meetings indicate countless of opportunities to monitor and review management performance (Hsu & Petchsakulwong, 2010). This is consistent with the statement of Evans, Evans and Loh

(2002) who claimed that the board of directors often increase their board meetings to solve problems relating to the firm's poor performance.

Moreover, Jackling and Johl (2009) and Lipton and Lorsh (1992) stated that the higher the meetings frequency is, the more the firm is likely to perform better. This is supported by Conger, Lawler and Finegold (1998) and Kyereboah-Coleman (2007) who claimed that board meeting time is a key resource for improving the effectiveness of corporate board.

The result of foreign member on the board (BOFOREIGN) in Table 6.7 shows the mean value of the foreign members on the board in the Omani Stock Market is 26 % with a minimum zero (0) and a maximum one hundred percent (100%). Both the agency theory and the resource dependence theory postulate that the diversity of the board in terms of nationality may enhance monitoring for better performance. Similarly, Oxelheim and Randoy (2003) revealed that foreign board members positively and significantly impacts firm performance. According to them, having a foreign board member indicates greater commitment to monitor management, transparency and improved reputation in the financial market which results in superior value of the firm. In the context of family firms, foreign directors can bring valuable knowledge, expertise, and board efficient monitoring.

Foreign directors offer invaluable knowledge regarding contextual issues in foreign markets and they contribute to the facilitation of strategic decision making quality (Zahra

& Filatotchev, 2004). Foreign directors are also considered to take along with them invaluable expertise and diversity, particularly in companies that have global operations. With regards to countries having weak legal and governance institutions, the importation of directors may enhance the level of the firm and minimise cost of capital by reflecting its inclination to employ higher governance standards of the foreign directors' home country (Miletkov, Poulsen & Wintoki, 2011). The Omani Code of Corporate Governance (2002) stated that companies are free to appoint foreigners in the firm and this serves to improve firm performance.

With reference to audit committee size (ACSIZE), the result in Table 6.7 indicates that the mean of audit committee size is about four (4) members with a minimum of two (2) members and a maximum of seven (7) members. The audit committee size of the sample in this study was not much different from the studies by Al-Matari *et al.* (2012a, 2012b) and Ghabayen (2012) in Saudi Arabia, which is three (3) members and Al-Matari *et al.* (2012) in Kuwait, which is also three (3) members. Concerning the Corporate Governance Code (2002) in Oman, the audit committee should consist of at least three members and this is supported by Fama and Jensen (1983) who claimed that three members are essentially good for the performance of the firm. Meanwhile, Jensen and Meckling (1976) stated that the audit committee is among the main elements of CG system that plays a crucial role in administering the internal control framework effectiveness and the financial reporting review of the firm. It is an intermediary among

internal auditors, external auditors, management and board of directors in establishing the effective information flow and transparent reporting.

Moreover, among the primary roles of the audit committee is to assure the quality financial reporting and control systems. The audit committee is considered to be one aspect of monitoring mechanisms which is available for the reduction of information asymmetry between insiders and outsiders (Kim & Yoon, 2007). The audit committee is also the most dependable mechanism that works to safeguard the interests of the public (Abdurrouf, 2011; Kyereboah-Coleman, 2007).

The result in Table 6.7 also indicates that the mean of audit committee independence (ACINDE) is about 93 % with a minimum of zero and a maximum of 100 %. This result indicates that MSM companies are in line with international codes such as the Cadbury Committee (1992), the Blue Ribbon Committee (BRC, 1999), the Sarbanes-Oxley Act (2002), the Organisation for Economic Cooperation and Development's (OECD, 2004) and the Code of Corporate Governance (2002) in Oman which requires that the majority of the audit committee must be independent. This study was not similar with studies such as and Al-Matari *et al.* (2012b) in Saudi Arabia, which revealed 78 %. This factor is essential for the corporate governance, based on Swamy's (2011) study claiming that non-executive members in the committee has a key role in ensuring that CG practices of auditing complied with impact the financial report. As a result, audit committees with the higher members of non-executive directors were considered to be more independent

when compared to their counterpart committees with higher executive directors (Rahmat *et al.*, 2009).

For audit committee meeting (ACMEETIN), the results in Table 6.7 indicate that the mean of the audit committee meeting is about five (5) times a year with a minimum of zero (0) and a maximum of ten (10) times per year. This result is consistent with the guidelines provided by the Cadbury Committee (1992) in the UK and the BRC (1999) in the US. The guidelines mandate audit committees to hold meetings not less than three times in a year. This is consistent with the Omani Code of Corporate Governance (2002) that mandates the committees to hold the meetings, at least four times yearly with a majority of independent directors. This result is also similar with previous study done by Al-Matari *et al.* (2012b) in Saudi Arabia, which is five (5) times per year. This significant factor shows a strong implementation of good CG, which in turn enhances company performance. Similarly, frequent and monitored meetings would be of value in assisting audit committees in their examination of accounting and internal control systems and relaying the committee's actions to the top management (McMullen & Raghunandan, 1996).

With regards to firm size (FIRMSIZE), the outcome in the Table 6.7 shows that mean of the firm size is about (49181392) OMR with a minimum of (605320) OMR and a maximum of (685377000) OMR. In this regard, Patro, Lehn and Zhao (2003) stated that both firm size and growth are key determinants of board size and structure. In addition, firm size affects firm performance and is often employed as a control variable in the

empirical literature dedicated to CG (e.g. Andres *et al.*, 2005; Ghosh, 2006; Yan *et al.*, 2007).

As for leverage (LEVERAGE), the result in Table 6.7 indicates that the mean of leverage is about 0.48 with a minimum of 0.02 and a maximum of 1.72. The debt ratio impacts the outcomes of the firm where a positive impact may result in minimised cash flow and company control. On the basis of the agency theory (Jensen & Meckling, 1976), the firm should have to support its monitoring costs including its increasing debt level.

Finally, in the performance measures, the mean of ROA is 0.07 with a minimum of -0.48 and a maximum of 1.631. The standard deviation is 0.13 indicating a narrow variation in the ROA across the companies in the sample. On the other hand, the mean of Tobin-Q is about 1.29 with a minimum of 0.27 and a maximum of 3.92. The standard deviation is 0.57. This shows that there is a small variation in the Tobin-Q across the firms in the sample.

6.5 Correlation Analysis

In this study, the correlation analysis was carried out. Since Pallant (2011) stated that correlation analysis is useful in describing the strength and direction of the linear relationship between two variables. More specifically, the Pearson correlation analysis was employed to assess and clarify the strengths of the relationship among the study variables as provided in Table 6.8. The correlation coefficient (r) values provided in the Table 6.8 shows the strength of the relationship among variables and in determining this

strength. Hair *et al.* (2010) recommended that the correlation value of 0 shows no relationship, while the correlation ± 1.0 shows perfect relationship. Cohen (1988), on the other hand, interpreted the correlation between 0 and 1.0 as follows; the correlation (r) between ± 0.1 and ± 0.29 shows small relationship, between ± 0.30 and ± 0.49 shows medium relationship and above ± 0.50 shows strong relationship.

Generally, the result of this study shows that all correlations are less than 0.80. This is consistent with the statement of Gujarati and Porter (2009) that the correlation matrix should not exceed 0.80 to ensure that the multicollinearity issue is not present in this study. The next step is to determine the VIF in Table 6.9 where a VIF more than ten shows a multicollinearity issue (Hair *et al.*, 2010). The values of VIF were reported and found to be ranging from 1.05 and 2.00, which shows the non-existence of the multicollinearity issue.

The firm size (FIRMSIZE) is positively related to ROA at the 0.01 level. On the contrary, leverage (LEVERAG) has a strong negative relation with ROA at the 0.01 level. Furthermore, the outcome in the Table 6.9 indicates that board size (BOARDSIZE), board independence (BORADIN), board meeting (BOARDME), audit committee size (ACSIZE), audit committee independence (ACINDE) and audit committee meeting (ACMEETIN) have a positive relation to the return on assets (ROA) but not significant. On the other hand, foreign member (BOFOREIGN) has a negative relation with ROA but not significant.

In measuring the association between all the variables and the Tobin-Q, as another measure of firm performance, it was found that board size (BOARDSIZE) has a positive significant relation with Tobin-Q at the 0.01 level. On the other hand, board independence (BORADIN) and audit committee meeting (ACMEETIN) have a strong negative relation with Tobin-Q at the 0.01. In the same line, audit committee independence (ACINDE) and leverage (LEVERAG) have a strong negative association with Tobin-Q at the 0.05. In addition, board meeting (BOARDME) and firm size (FIRMSIZE) have a positive relation with Tobin-Q, but it is not significant. On the other hand, foreign member (BOFOREIGN) and audit committee size (ACSIZE) were found to be negatively but not significantly related with Tobin-Q.

Table 6.8
Results of Pearson Correlation Analysis

	1	2	3	4	5	6	7	8	9	10	11
1) BOARDSIZE											
2) BORADINDE	-0.022										
3) BOARDME	-0.008	0.1**									
4) BOFOREIGN	-0.053	-0.170***	-0.217***								
5) ACSIZE	0.426***	0.148***	0.134***	-0.215***							
6) ACINDE	-0.044	0.677***	0.116**	-0.134***	0.065						
7) ACMEETING	-0.015	0.163***	0.487***	-0.225***	0.058	0.131***					
8) FIRMSIZE	0.289***	-0.011	0.114**	-0.012	0.160***	0.093	0.085				
9) LEVERAGE	-0.123**	-0.073	-0.099*	0.299***	-0.117**	-0.061	-0.028	-0.069			
10) ROA	0.047	0.015	0.042	-0.072	0.056	0.082	0.070	0.133***	-0.331***		
11) TOBINSQ	0.165***	-0.208***	0.045	-0.066	-0.014	-0.117**	-0.167***	0.082	-0.125**	0.222***	

Notes:

*** Correlation is significant at the 0.01 level (2- tailed).

** Correlation is significant at the 0.05 level (2- tailed).

* Correlation is significant at the 0.1 level (2- tailed).

6.6 Panel Data Analysis

One of the most commonly used statistical methods in many applications of science disciplines is the regression analysis (Hair *et al.*, 2010). According to DeCoster (2004), a regression is a statistical method allowing the researchers' prediction of the value of one variable from one or more other variables. He stated that when the regression analysis is performed, a regression equation predicting the dependent variable's value through the values of the independent variables arises.

Therefore, in this study, linear regression analysis was employed to determine the direct relationship between independent variable and dependent variable and to determine the relationship direction. According to Pallant (2011), linear regression can be employed for the prediction of the value of the single continuous dependent variable from a single continuous independent variable.

Multivariate regression analysis was used to establish the relationship between independent variables and the dependent variable and to identify the direction of the relationship. It reflects the level to which a set of variables is capable of predicting a specific outcome. It is also a multivariate statistical method that can be utilised to investigate the relationship between independent variables and a single dependent variable.

Data was first examined to meet the many multivariate assumptions prior to running multivariate regression analysis and to establish the reliability of the conclusions drawn. The primary assumptions that were examined prior to the regression analysis include linearity, normality, homoscedasticity and the independence of the error terms. Prior to assumptions testing, the study investigated the presence of multicollinearity and outliers.

On the basis of the discussion of results, it was concluded that the statistical assumptions needed for multivariate statistical method were met and that satisfaction of these assumptions guarantees valid and reliable results. The testing of these assumptions along with regression analysis is further discussed in detail in the coming sub-sections.

Prior to carrying out the multivariate regression analysis, outlier, normality, checking, linearity, heteroscedasticity, contemporaneous, correlation and autocorrelation presence was examined. No serious issues related to both were detected. The investigations also showed that all the required criteria for regression analysis were met. The following procedures were employed in the study.

6.6.1 Outlier Detecting

Outliers are considered as observations having unique features that significantly differ from others (Hair *et al.*, 2010). Outliers can be determined through the use of univariate, bivariate and multivariate methods on the basis of the number of variables. The most commonly employed method for the detection of outliers is Mahalanobis Distance Measure. It is a method that measures the distance of every observation from the mean

centre of all observations in a multidimensional space (Hair *et al.*, 2010). The detection of outlier observations requires the examination and comparison of Mahalanobis distance values to the Chi-square distribution table.

The present study's results show that the Mahalanobis distances of the entire observations are ranging between 5.086 and 65.371. On the basis of the Chi-Square distribution table, the critical value at the level of significance of 0.001 and 11 degrees of freedom is 31.26 which indicate the presence of outliers. For the identification of outliers, further examination through the SPSS package saved in the data as Mahalanobis distance was compared to 31.26. As a consequence of this comparison, fifteen observations of Mahalanobis distances found to range from 31.52 to 65.37 were deemed as outliers.

The analysis of the regression model was performed with and without their value and the results showed no significant changes and thus, the researcher retained them. In the preceding sections, the diagnostic test was employed among study variables.

6.6.2 Diagnostic Tests

To guarantee data quality, prior to running multivariate regression analysis, key assumptions related to multivariate regression analysis have to be examined. These have to be satisfied to ensure that the actual errors in prediction of the model stem from the actual absence of associations among variables and not from data characteristics that failed to be accommodated by the regression method (Hair *et al.*, 2010). These assumptions include multicollinearity, linearity test, the absence of heteroscedasticity,

contemporaneous correlation, autocorrelation (Hair *et al.*, 2010; Gujarati, 2003) and all of them were tested in this study as follows.

6.6.2.1 Normality

Normality refers to the data distribution shape for individual quantitative data variable and its normal distribution. In multivariate analysis, it is basically assumed that a significant deviation from such normality will lead to invalid statistical results (Hair, Black, Babin, Anderson & Tatham, 2006). In this regard, the residual refers to the difference between the observed and predicted values, where independent and the normal distribution is expected. Accordingly, in this study, the researcher conducted an assessment for normality testing residuals. If the residuals are aligned with the assumption, then the individual variables normality requires examination (Tabachnick & Fidell, 2007). The most extensively utilised normality tests are skewness and kurtosis. Skewness is described as the balance of distribution where an abnormally distributed skewness has a notable shift to either the left or the right. On the other hand, kurtosis is the peakedness or flatness of a distribution relative to the normal distribution. The use of kurtosis and skewness in statistical tests show sensitivity to data of considerable size (Tabachnick & Fidell, 2007). A variable displaying skewness or kurtosis does not often show significant deviation from normality – in other words, it does not always affect the analysis in a significant way. The distribution shape can be noted on a plotted graph (Tabachnick & Fidell, 2007). According to standardised normal probability plots

(pnorm), the residual distributions were noted and are sensitive to non-normality in the middle of the data range.

Similarly, in Miller's (1997) study the residual was noted against the normal distribution quartiles (sensitive to non-normality near the tails). Normal probability plot is an accurate method because actual data values are compared with the cumulative values of normal distribution (Hair *et al.*, 2006). Normality is indicated by a line showing actual data following normal distribution or diagonal line. This study examined the normality plot of ROA and Tobin-Q models and showed a minor deviation from normality. Because the present study's sample is larger, this condition may not affect the results as according to Hair *et al.* (2006), considerable deviation from non-normality may be overlooked for a sample size of 200 or over.

6.6.2.2 Checking the Multicollinearity

Multicollinearity is considered as the level to which the impact of any variable can be explained by other variables (Hair *et al.*, 2010). An increase in multicollinearity increases the difficulty in interpreting the effects of different variables. This study employed the tolerance value and VIF to investigate the existence of multicollinearity among the study variables. Tolerance is the variability in a variable that is not explained by other variables (Hair *et al.*, 2010). The VIF indicator is the reciprocal element of tolerance variable.

The tolerance values of the present study's variables are presented in Table 6.10 and they ranged between 0.50 and 0.95 while the VIF values ranged between 1.05 and 2.00

indicating that all the tolerance values were higher than 0.1 and VIF below the threshold of 10 as recommended by Hair *et al.* (2010). Stated differently, both the tolerance and VIF values of the variables are within the recommended range. It can thus be concluded that the multicollinearity issue is non-existent.

Table 6.9
Multicollinearity Test

Variables	VIF	1/VIF
Board Size (BOARDSIZE)	1.40	0.72
Board independence (BORADINDE)	2.00	0.50
Board Meeting (BOARDME)	1.40	0.72
Board Change (BOARDCH)	1.05	0.95
Secretary (SECRETA)	1.14	0.87
Legal Counsel (LEGALCO)	1.13	0.89
Foreign Member (BOFOREIGN)	1.36	0.73
Audit Committee Size (ACSIZE)	1.39	0.72
Audit Committee Independence (ACINDE)	1.97	0.51
Audit Committee Meeting (ACMEETIN)	1.37	0.73
Executive Committee Existence (ECEX)	1.24	0.81
FIRM SIZE (FIRMSIZE)	1.25	0.80
Leverage (LEVERAG)	1.17	0.85
Industry (INDUSTRY)	1.17	0.85
Mean VIF	1.36	

Table 6.9 shows the tolerance values for the independent variables; which are above 0.10 and the VIF values are below the cut-off of 10. Hence, the assumption with regards to the absence of multicollinearity was not violated. It is therefore concluded that the present study is free from outliers and multicollinearity.

6.6.2.3 Checking of Linearity

The multivariate regression analysis considers a linear relationship between the dependent and predictor variables. Linearity is confirmed through the residual plots, but as this is not considered a scientific method, scholars have brought forward other methods.

In this regard, scholars brought forward several techniques. For instance, Hair *et al.* (2010) negated the issue of nonlinearity if the standard deviation of the dependent variables is greater than that of residuals. The standard deviation of the dependent variables presented in Table 6.10 shows that they are higher compared to that of the residuals indicating that nonlinearity is not an issue.

Table 6.10
The Standard Deviation of Firm Performance and the Residuals

Variable	Std.Dev.	Residuals
ROA	0.138	0.127
TQ	0.5714	0.520

6.6.2.4 Checking of Heteroscedasticity

Heteroscedasticity or what is commonly known as the unequal variance is considered one of the common violations. It is assumed in multivariate analysis that the residuals in a regression specification are homoscedastic (equally spread or with equal variance). Heteroscedasticity appears with any increase or decrease of the variance and this leads to statistical inference problems in the regression model. The homoscedastic assumption has

to be examined prior to applying regression analysis on the results. Heteroscedasticity can be detected through graphical tests where, the residuals of the model are plotted against the predicted value of firm performance and every explanatory variable to identify whether or not the model's error terms possess constant variances.

The Breusch-Pagan/Cook-Weisberg Test results are displayed in Table 6.11. Based on the results, the p-value is higher than 0.05 for ROA indicating that the model accepts the null hypothesis and no issue of heteroscedasticity exists. Contrastingly, for Tobin-Q, the p-value is less than the threshold (0.05) and thus, in this case the model rejects the null hypothesis and highlights a heteroscedasticity issue. The results indicate variability in variance that needs to be corrected.

The issue of heteroscedasticity is handled with the help of White Heteroscedasticity Consistent Variance and Standard error technique as recommended by Gujarati (2003). Such a test is carried out through STATA (version 12) software. The above method decreases or increases the standard error as needed and the fluctuations lead to the respective decrease or increase of t-statistics with the coefficient remaining constant. The results do not significantly differ from the prior regression with slight changes in the t-statistic and p-values to present the estimator's correction.

Table 6.11
Breusch-Pagan/Cook-Weisberg Test

	chi2	Prob > chi2
ROA	1.39	0.24
TQ	112.42	0.00
Ho (null)	Accepted	Rejected

Note: Ho (null): Constant variance (homoscedasticity), ROA=Return on assets, TQ=Tobin-Q.

6.6.2.5 Checking of Contemporaneous Correlation

Contemporaneous correlation, also referred to as cross-sectional dependence, is the correlation of unobserved factors throughout the units. This correlation has a tendency to rise in a sample having cross-section units (Wooldridge, 2003). The significant interdependencies among cross-sectional units can stem from the economic and financial factors included in state and financial entities. Hence, an identical reaction may be experienced by individuals according to their interdependent preferences, neighbourhood effects, herd behaviours and social norms. Oversight of the presence of this correlation may lead to standard error estimation bias.

STATA (version 12) was employed to test cross-sectional dependence with the help of *xtcds*, *pesaran* syntax, which is applicable for large N and small T panel data (Hoyos and Sarafidis, 2006). This process involves the application of a parametric testing procedure recommended by Pesaran (2004). Specifically, the test was conducted on the two regression models, namely accrual based ROA and Tobin-Q and showed that there is no issue regarding testing.

Table 6.12
Pesaran's Test

	Pesaran's test of cross sectional independence	Average absolute value of the off-diagonal elements
ROA	3.913, Pr = 0.00	0.45
TQ	2.566, Pr = 0.01	0.47

6.6.2.6 Checking of Autocorrelation

The function of autocorrelation can be employed to resolve the query of whether or not the sample data set is produced from a random process. It is expected that the residual terms of any two cases should not be correlated but rather independent. Autocorrelation is considered to be present where residual terms are not independent (Field, 2000). In addition, autocorrelation violates the assumption that errors are uncorrelated and independent and that both size and direction of a single error term does not influence on the size and direction of another, or notation wise, OLS assumes: $E(\epsilon) = 0$. Autocorrelation can be related to cross-sectional data, although it is often related to time series data. By definition, the latter is ordered in time (the difference is noted by t indexing). As the past is the best predictor of the future, it is contended that what happens in time t best predicts what will happen in time $t+1$. Intrinsically, observations are not often independent. With regards to the error term, this indicates the differences between the predicted and actual error at one point in time and its relation to the next error. The errors can be negatively correlated in cases where the series is mean-reverting.

Autocorrelation may also be caused by the misspecification of the model and manipulation of data. In the time series, data is aggregated and a specific level of smoothing is introduced through the creation of a quarterly data set by summing up or taking the average over the months. Hence, some of the disaggregated data's randomness is dissipated. Such smoothing can result in systematic patterns in the error terms and possible autocorrelation.

Autocorrelation can be detected in various ways with one of them using the Wooldridge Test. This test examines for serial correlation in random or fixed-effects one way models obtained by Wooldridge (2002). In turn, Drucker (2003) employed the Wooldridge Test in his determination of serial correlation in the idiosyncratic error term in the panel-data model. Autocorrelation may also be determined through the use of Durbin-Watson test.

Table 6.13
Wooldridge Test

	F (1,77)	Prob > F
ROA	0.45	0.50
TO	34.78	0.00
H0	Accept	Reject

Note: Ho (null): No first-order autocorrelation, ROA=Return on assets and TQ=Q=Tobin-Q.

From the results in Table 6.13, the Wooldridge Test was conducted to see whether there is an autocorrelation problem in the data with ROA. However, in this study, the researcher

made use of the Wooldridge test to determine whether or not autocorrelation issue exists in the data with Tobin-Q after which a positive autocorrelation was highlighted.

Another way to determine if autocorrelation exists is, by using the Durbin-Watson (DW) test. The DW test is employed as a statistical test for the detection of autocorrelation and Reinard (2006) and Kazmier (1996) claimed that the value of the test statistics may differ from 0-4.0. If the value of the statistic is lower than 1.4, this indicates the presence of a significant positive series of correlation, and if the value is higher than 2.6, this indicates the presence of significant negative series of correlation (Kazmier, 1996). The rule of thumb stipulates that DW should be within the acceptable range of 1.5 to 2.5.

Table 6.14
Durbin-Watson Test

Variable	Value of Durbin-Watson
ROA	1.87
TQ	1.9

Tables 6.14 show the result of the autocorrelation test, in which the DW value of 1.87 and 1.9 falls in the acceptable range of 1.5 to 2.5, indicating the independence of observations. Based on the above discussion, this study used GLS to correct heteroscedasticity and autocorrelation noted in Tobin-Q.

6.7 Results of LM Test

The step involves the performance of the Breusch-Pagan LM test in order to compare between the OLS and RE model. The primary difference between the two models being

their consideration of individual effects. Hence, a statistical test can be created on the basis of the notion of the presence or absence of u_i – denoting random effect. For this determination, the Breusch-Pagan LM test is appropriate. The test is primarily based on the idea that if u_i is equal to zero for the entire i 's, then there is no individual heterogeneity and this indicates that the pooled OLS model is suitable to be used. If on the other hand, the LM test generates significant chi-square value, indicating a low p-value that is less than 0.05, the null hypothesis rejects pooled estimates suitability. Hence, the random effects method is preferred over the pooled OLS.

Table 6.15
LM Test

	Test: Var(u)	chibar2(01)	Prob > chibar2
ROA	0	51.08	0.00
TQ	0	322.07	0.00
H0	Rejected	Rejected	Rejected

Based on Table 6.15 which shows that the $\text{prob} > \text{Chi}$ is positive at 0.00 level larger than 0.05 so, it is safe to use random effects.

6.8 Results of F Test

The restricted F-test is first conducted to carry out a comparison between the pooled OLS and the FE models, where the primary distinction between them lies in the premise of the individual effects. While the OLS claims no individual heterogeneity, the FE model claims individual heterogeneity and it is associated with a single or more regressors. This indicates the use of the restricted F-test with a low p-value of less than 0.05. Fixed effects

are opted for rather than pooled OLS as the null of no individual effect is rejected and there is no evidence supporting the presence of individual effects. For this reason, the FE model is selected.

Table 6.16

F Test

	Test statistic:	with p-value
ROA	F(77, 299) = 2.76204	P(F(77, 299) > 2.76204) = 3.66719e-010
TQ	F(77, 299) = 10.8438	P(F(77, 299) > 10.8438) = 1.16415e-052
H0	Rejected	Rejected

Table 6.16 displays that the p-value is positive and larger than 0.05 hence, it is safe to use fixed effects.

6.9 Results of Hausman Test

Greene (2008) stated that the assumption underlying the random effects model concerning the absence of correlation of individual effects with other regressors lack justifying evidence. Hence, it may contain inconsistency when such correlation is present. As mentioned, the primary factor distinguishing fixed effects from random effects is if the error term is associated with independent variables and, on this basis the choice between fixed effects method and random effects method of panel data regression involves the determination of the correlation through the Hausman specification test. Keeping in mind that the fixed effects model considers the presence of correlation between independent variables and error term, whereas the random effects model does not, the following hypotheses are formulated;

H0: Unobserved effect is uncorrelated with explanatory variables.

H1: Unobserved effect is correlated with explanatory variables

The null hypothesis assumes the use of random effects and the first hypothesis assumes the use of the fixed effects. The Hausman specification test is used when running the models to examine whether or not there is a correlation between the explanatory variables and the error term (Baltagi, 2008). If a significant p-value is generated, the null hypothesis is rejected and the fixed effects model is opted. In the present study, the researcher performed two Hausman tests, with one test for the ROA and other for Tobin-Q. The Hausman tests on the two models showed significance at the level of 1% and thus, the null hypothesis was rejected. Therefore, based on the test, this study used random effect to analyse panel data.

According to Greene (2003), the regression model takes the form of random effect model in order to realise a balanced panel data. The random effect model was more appropriate to the data set opposed to its fixed effect counterpart, as controlling the effect of the industrial sectors on the firm's performance was necessary. The latter model does not allow for such control because industrial dummy remains constant over time. The estimation model employed for the examination of the corporate governance-firm performance relationship is presented as follows:

Table 6.17
Hausman Test

	chi2(13)	Prob>chi2
ROA	5.39	0.97
TQ	7.36	0.88
H0	Reject	Reject

Regarding the result found in Table 6.17 which shows that both ROA and Tobin-Q are not significant p-value. Meaning that reject fixed effect and accepted random effect. Thus, this study adopted random effect to analyse panel data.

6.10 GLS estimation

The present study makes use of the panel data regression to test the equation of the proposed models. Panel data method is used as it enables the deletion of the unobservable heterogeneity that various firms in the sample data could generate (Himmelberg, Hubbard & Palia, 1999). In fact, panel data regression is invaluable since it is more beneficial compared to cross-sectional or time-series regression's independent application. The benefits include; the combination of time-series and cross-sectional observations, generation of informative data, variability, less variables collinearity, higher levels of freedom and higher efficiency. Also, making data accessible to several thousand units can lessen the bias that may stem if individual company data is categorised into broad categories. Finally, panel data can accurately confirm and measure impacts that are unobservable in case of pure cross-section or pure time-series data method (Gujarati, 2003; Baltagi, 2001).

It is assumed by the classical normal linear regression that the error term remains constant over a period and location. The truth behind such assumption would confirm the existence of homoscedasticity. Nevertheless, various interpretations have been attributed to the observation. The first being that this may lead to the variable error term variance generated from the regression and to the presence of heteroscedasticity. If this happens, the dependent variable's estimates may not be as predictable (Gujarati, 2003). OLS estimation, unlike GLS is not able to solve this issue as it employs the premise of minimisation (sum of residuals squares). Under this method, every error term is provided with identical weight, although some of them are much nearer to the functions of the sample regression. Stated clearly, the entire errors are given equal importance regardless of their proximity from the sample regression function.

On the other hand, the GLS lessens the weighted sum or residual squares and assigns each error term weight that is in proportion to its σ^2 (error term variance). Hence, an error term that arises from a population with a larger σ^2 will receive a proportionate weight in lessening the residual sum of squares (RSS). The notion lies in providing less weight to an error term that has close proximity to the mean compared to those that are scattered further. The GLS handles this issue by providing the appropriate weight to error terms and thus producing ideal constant variance. This consideration of the non-constant error term enables GLS to produce estimators like the Best Linear Unbiased Estimators (BLUE) (Gujarati, 2003). Based on results that there are positive Heteroscedasticity and autocorrelation with Tobin-Q, this study used GLS to solve this problem.

6.11 Model Estimation

The present study made use of the generalised least square (GLS) over the five year period as opposed to the ordinary least square (OLS) because the latter's use would be optimal if there are cross-sectional uncorrelated residuals and if there is homoscedasticity throughout firms (Baltagi, 2001). In other words, the OLS estimates may be unbiased and consistent under the normality and constant variance violation, but they are inefficient, with estimated standard errors that are biased and inconsistent. As such, GLS is more applicable as it standardises the observations (Baltagi, 2001; and Greene, 2003). In addition, GLS is also capable of running data regression with normality problems. The GLS is considered as the OLS on the transformed variables that does not go against the assumptions of the standard least square (Gujarati, 2003). Because the coefficients will be constant throughout the period, the estimation through panel regression is efficient. This estimation can also be utilised to determine the results sensitivity towards other specifications (Gujarati, 2003).

6.12 Evaluation of the Models

Following the testing of the regression assumptions, the researcher conducted regression analysis using Stata version 12 to examine the predictive power of board of directors' characteristics (board size, board independence, board meeting, board change, secretary role, legal counsel and foreign member on the board), audit committee characteristics (size, independence and meeting), executive committee and their dimensions towards the

firm performance. The main purpose of the carried out multivariate regression analysis was to determine the predictive power of each independent variable towards the dependent variable.

This part is divided into two sub-sections. The first sub-section examines the relationship between board of directors' characteristics (board size, board independence, board meeting, board change, secretary role, legal counsel and foreign member on the board), audit committee characteristics (size, independence and meeting), executive committee and firm performance as measured by ROA. The second sub-section examines the relationship between the board of directors' characteristics (board size, board independence, board meeting, board change, secretary role, legal counsel and foreign member on the board), audit committee characteristics (size, independence and meeting), executive committee and firm performance as measured by Tobin-Q.

6.12.1 Model 1 (ROA as Dependent Variable)

In examining the hypotheses model through a multivariate regression analysis, some indicators are employed. Among them is R^2 (R Square) Coefficient, which evaluates the goodness of the regression equation. It is also referred to as the coefficient of determination that reflects the level of variance of the dependent variable that is explained by the model variables. In the present study, the researcher makes use of R^2 to show the amount of variance the dependent variable (ROA) that is explained by some of the dependent variable (firm performance as measured by ROA) resulting from the joint

effect of independent variable namely board of directors' characteristics (board size, board independence, board meeting, board change, secretary role, legal counsel and foreign member on the board), audit committee characteristics (size, independence and meeting), executive committee. According to the literature, if R^2 is equal to 1 that it means that there is a perfect linear relationship between the dependent and the independent variables. On the other hand, if R^2 is equal to 0, this means that there is no linear relationship existing between the dependent and independent variables. As a result, the value under R^2 shows the level of variance in the dependent variable (firm performance as measured by ROA) is explained by the model (which includes the variables of board of directors' characteristics (board size, board independence, board meeting, board change, secretary role, legal counsel and foreign member on the board), audit committee characteristics (size, independence and meeting) and executive committee.

As revealed by the results in Table 6.18, the value of R^2 in this model is 0.164. This means that the model explains 16.4 % of the variance in firm performance as measured by ROA. This is considered a respectable result. The STATA (version 12) provides adjusted R^2 value in the output. In cases where there is a small sample, R^2 value is a rather optimistic overestimation of the actual population value (Tabachnic & Fidell, 2007). R^2 indicates that 0.164 per cent of the variation in the dependent variable is explained by the variations in the independent variables. This means that the variation in firm performance, as measured by ROA, was statistically explained or accounted for by

the regression equation. The results in Table 6.18 also show that this model is significant ($p < 0.01$) indicating the validity of the model used.

In order to test the hypotheses, standard beta coefficients were utilised. Standardised required the values of each different variables to be converted to the same scale for comparison of which beta value is the highest (while ignoring the negative signs). In this way, the standardised beta coefficients can be compared to one another with the larger coefficient indicating the stronger impact of the variable on the dependent variable. The regression coefficient revealed that the variables were predictors of the model's dependent variable.

In this model, the largest beta coefficient was (-0.188) which is leverage (LEVERAGE). This means that this variable made the strongest unique contribution to explain the dependent variable. Leverage (LEVERAGE) was also found to be significant at the 0.01 level of significance ($p < 0.01$). Therefore, this variable made a significant unique contribution to the prediction of the dependent variable (firm performance as measured by ROA). Moreover, the beta coefficient value for secretary role (SECRETETA) was slightly less than the beta of leverage ($p < 0.05$) ($\beta = -0.029$, $p < 0.05$). In addition, the time period (2011) was somewhat less than the coefficient of secretary role (SECRETETA) ($\beta = -0.033$, $p < 0.01$).

On the other hand, board size (BOARDSIZE) ($\beta = -0.000$, $p > 0.1$), board independence (BORADINDE) ($\beta = -0.015$, $p > 0.1$), board meeting (BOARDME) ($\beta = -0.002$, $p > 0.1$),

board change (BOARDCH) ($\beta=-.002$, $p>0.1$), legal counsel (LEGALCO) ($\beta=0.018$, $p>0.1$), foreign member on the board (BOFOREIGN) ($\beta=0.03$, $p>0.1$), audit committee size (ACSIZE) ($\beta=0.006$, $p>0.1$), audit committee independence (ACINDE) ($\beta=0.032$, $p>0.1$), audit committee meeting (ACMEETIN) ($\beta=.007$, $p>0.1$), executive committee existence (ECEX) ($\beta=-0.019$, $p>0.1$), firm size (FIRMSIZE) ($\beta=0.009$, $p>0.1$), industry (INDUSTRY) ($\beta=.006$, $p>0.1$) and time period ($\beta=0.004$, $p>0.1$), ($\beta=0.029$, $p>0.1$), ($\beta=-0.048$, $p>0.1$) failed to make a significant contribution as dependent variable predictors (firm performance as measured by ROA) because the significance values are greater than 0.1.

In sum, the results in Table 6.18 showed those two variables were revealed to be significant firm performance predictors (as measured by ROA). These variables are leverage (LEVERAGE) ($\beta=-0.188$, $t=-1.65$, $p<0.01$), secretary role (SECRETETA) ($\beta=-0.029$, $p<0.05$) and time period (2011) ($\beta=-0.033$, $p<0.1$).

However, other variables such as board size (BOARDSIZE) ($\beta=-0.000$, $p>0.1$), board independence (BORADINDE) ($\beta=-0.015$, $p>0.1$), board meeting (BOARDME) ($\beta=-0.002$, $p>0.1$), board change (BOARDCH), legal counsel (LEGALCO) ($\beta=0.018$, $p>0.1$), foreign member on the board (BOFOREIGN) ($\beta=0.03$, $p>0.1$), audit committee size (ACSIZE) ($\beta=0.006$, $p>0.1$), audit committee independence (ACINDE) ($\beta=0.032$, $p>0.1$), audit committee meeting (ACMEETIN) ($\beta=.007$, $p>0.1$), executive committee existence (ECEX) ($\beta=-0.019$, $p>0.1$), firm size (FIRMSIZE) ($\beta=0.009$, $p>0.1$), industry (INDUSTRY) ($\beta=.006$, $p>0.1$) and time period (2009, 2010 and 2012) ($\beta=0.004$, $p>0.1$).

($\beta=0.029$, $p>0.1$), ($\beta=-0.048$, $p>0.1$) were revealed to be statistically insignificantly related to the companies' firm performance (ROA).

Table 6.18
Regression Results of Model 1 (Dependent= ROA)

Variables	Coef	P>
Board Size (BOARDSIZE)	-.000	0.919
Board independence (BORADINDE)	-.015	0.767
Board Meeting (BOARDME)	-.002	0.58
Board Change (BOARDCH)	-.002	0.852
Secretary (SECRETA)	-.029	0.034**
Legal Counsel (LEGALCO)	.018	0.179
Foreign Member (BOFOREIGN)	0.031	0.396
Audit Committee Size (ACSIZE)	.006	0.636
Audit Committee Independence (ACINDE)	.032	0.516
Audit Committee Meeting (ACMEETIN)	.007	0.223
Executive Committee Existence (ECEX)	-.019	0.257
FIRM SIZE (FIRMSIZE)	.009	0.199
Leverage (LEVERAG)	-.188	0.000***
Industry (INDUSTRY)	.006	0.766
2009	-0.004	0.819
2010	0.029	0.11
2011	-0.033	0.072*
2012	-0.048	0.709
Number of obs		390
Number of group		78
Wald chi2(18)		53.19
R ²		0.164
Prob > chi2		0.000

Notes:

*** Correlation is significant at the 0.01 level (2- tailed).

** Correlation is significant at the 0.05 level (2- tailed).

* Correlation is significant at the 0.1 level (2- tailed).

6.12.2 Model 2 (Dependent Variable Tobin-Q)

Various tests of significance are employed to the multivariate regression analysis results. R^2 (R Square) Coefficient is an instrument used to evaluate the goodness of the regression model. R^2 is also referred to as the coefficient of determination that indicates the amount of variance of the dependent variable that is explained by the variables in the model. In this study, R^2 is used to indicate the share of the variance of the dependent variable (firm performance as measured by Tobin-Q) that is explained by the combined effect of independent variables, namely board of directors' characteristics (board size, board independence, board meeting, board change, secretary role, legal counsel and foreign member on the board), audit committee characteristics (size, independence and meeting), executive committee. If R^2 is equal to 1, it means that there is a perfect linear relationship between the dependent and the independent variables. On the other hand, if R^2 is equal to 0, it means that there is no linear relationship between the dependent and independent variables.

As presented by the results in Table 6.19, the value of R^2 in this model is 0.142. This means that the model explains 14.2 % of the variance in firm performance as measured by Tobin-Q. Moreover, R^2 value in the sample tends to be a rather optimistic overestimation of the true value in the population (Tabachnic & Fidell, 2007). This means that the variation in firm performance as measured by Tobin-Q was statistically explained or accounted for by the regression equation. The results in Table 6.19 also

show that this model was significant, since the F value was significant at ($p < 0.01$). Thus, indicating the validity of the model used.

Beta analysis is a technique utilised to show the significance of the regression coefficients while regression analysis is for the comparison of the relative effect of the independent variables on the dependent variable. For hypotheses testing, the researcher makes use of standardised beta coefficients. The term standardised implies that the values of each of the various variables are transformed to the same scale so comparison of which beta value is the highest becomes possible (ignoring negative signs). The standardised beta coefficients can then be compared to one another. The larger beta coefficients depict stronger variable impact on the dependent variable. The regression coefficient presents the variables contribution to the prediction of the dependent variables present in the model.

In this model, the largest beta coefficient was 0.114, which is the effect of the time period (2010). This means that this variable made the strongest unique contribution to explain the dependent variable. The time period was also found to be significant at the 0.05 level of significance ($p < 0.01$). Hence, this variable significantly contributes to the dependent variable's prediction (firm performance as measured by Tobin-Q).

The beta coefficient value for the executive committee existence (ECEX) ($\beta = -0.109$, $p < 0.1$), was slightly less than the beta of board independence (BORADIN) ($p < 0.01$). In addition, audit committee meeting (ACMEETIN) ($\beta = -0.062$, $p < 0.01$), the beta value for

the board size (BOARDSIZE) ($\beta = 0.067$, $p < 0.05$) was found to be a significant predictor of the firm performance as measured by the Tobin-Q. These variables significantly contribute in explaining the Tobin-Q.

On the other hand, board independence (BORADINDE) ($\beta = -0.352$, $p > 0.1$), board change (BOARDCH) ($\beta = 0.034$, $p > 0.1$), secretary (SECRETA) ($\beta = 0.001$, $p > 0.1$), legal counsel (LEGALCO) ($\beta = 0.008$, $p > 0.1$), foreign member on the board (BOFOREIGN) ($\beta = -0.216$, $p > 0.1$), audit committee size (ACSIZE) ($\beta = -0.030$, $p > 0.1$), audit committee independence (ACINDE) ($\beta = 0.1301$, $p > 0.1$), firm size (FIRMSIZE) ($\beta = 0.009$, $p > 0.1$), leverage (LEVERAG) ($\beta = -0.080$, $p > 0.1$), industry (INDUSTRY) ($\beta = -0.0876$, $p > 0.1$) and time period (2009, 2011 and 2012) ($\beta = 0.065$, $p > 0.1$), ($\beta = 0.01$, $p > 0.1$), ($\beta = -0.002$, $p > 0.1$) do not significantly contribute to the prediction of the firm performance (peroxided by Tobin-Q).

Table 6.19

Regression Results of Model 2 (Dependent= TobinQ)

Variables	Coef	P>
Board Size (BOARDSIZE)	0.067	0.022**
Board independence (BORADINDE)	-0.352	0.205
Board Meeting (BOARDME)	0.030	0.012 **
Board Change (BOARDCH)	0.034	0.379
Secretary (SECRETA)	0.001	0.986
Legal Counsel (LEGALCO)	0.008	0.840
Foreign Member (BOFOREIGN)	-0.216	0.135
Audit Committee Size (ACSIZE)	-0.030	0.386
Audit Committee Independence (ACINDE)	0.1301	0.561
Audit Committee Meeting (ACMEETIN)	-0.062	0.003***

Table 6.19 (Continued)

Variables	Coef	P>
Executive Committee Existence (ECEX)	-0.109	0.052*
FIRM SIZE (FIRMSIZE)	0.009	0.757
Leverage (LEVERAG)	-0.080	0.563
Industry (INDUSTRY)	-0.0876	0.486
2009	0.065	0.176
2010	0.114	0.026**
2011	0.012	0.856
2012	-0.002	0.966
Number of obs		390
Number of group		78
Wald chi2(18)		36.92
R ²		0.142
Prob > chi2		0.005

6.13 Hypotheses Testing

6.13.1 Model (1) and Result of Analysis

In this section, the results of the analysis of the relationship between firm performance (ROA) (dependent variable) and board of directors' characteristics (board size, board independence, board meeting, board change, secretary role, legal counsel and foreign member on the board), audit committee characteristics (size, independence and meeting), executive committee and firm size, leverage, industry and time period (a control variable) are presented through multivariate regression analysis.

6.13.1.1 Control Variables and ROA

The present study includes four control variables, namely firm size, leverage, industry and time period. The first of them is the firm size. The use of firm size as the control variable is justified by the findings of companies with various distinct characteristics. The possibility, that firm size and growth are significant determinants of board's size and structure, was highlighted by Patron, Lehn and Zhao (2003). According to them, firm size is directly related to its size and is inversely proportional the proxy of growth opportunities. In addition, the firm size affects firm performance and is widely utilised as a control variable in empirical studies dedicated to corporate governance (e.g. Andres *et al.*, 2005; Ghosh, 2006; Yan *et al.*, 2007). The influence of firm size on corporate governance has also been reported in findings that depict large companies to be less effective in comparison to their smaller counterparts because even though they adhere to government bureaucracy, they are riddled with ambiguity and higher agency problems (Patro *et al.*, 2003). The result in Table 6.20 shows a positive relationship, but statistically insignificant ($\beta=.009$, $p>0.1$) between firm size (FIRMSIZE) and ROA.

The second control variable considered was the debt ratio that refers to the total sum of long-term debt and short-term liability as the total assets percentage. Debt ratio impacts the outcomes of the company. A positive effect may result in minimised cash flow, and control of the company, which could depict more of the market. As illustrated in Table 6.20, the result shows a negatively significant relationship between leverage (LEVERAG) and ROA ($\beta=-.188$, $p<0.01$).

With regards to the third control variable, the industry that this study follows Firer and Williams (2003) study where industry is controlled through a dummy control variable. Akin to the year dummy variable, the nine dummy variables reflect the impacts of ten differing industries explained by the Global Vantage Economic Sector Code, with the industries ranging from high IC telecommunication firms to physical resource-based firms and utilities and materials industries. Every variable is coded '1' an observation relates to the industry that the variable is representing. Table 6.20 reveals that the industry sector was found to be insignificant determinant of the ROA ($\beta=.006$, $p>0.1$).

Finally, the fourth control variable that was considered in this study is the Time Period. The findings shown in Table 6.20 disclose that the performance among years is similar, except 2011 when a negative significant effect on the performance can be noticed. This is maybe affected by the evaluation that happened in the Middle East. Regarding this action, many investors transferred their economic activities to other safe countries. Therefore, Oman has become no more safe country regarding this situation. As a matter of fact, the investors need to invest their money in a safe environment and they are waiting to generate profit in the short term rather than long term. Table 6.20 shows that performing of companies is not significant during years except, 2011, that has been negatively significant (2009, 2010, 2011 and 2012) ($\beta=-0.004$, $p>0.1$), ($\beta=0.029$, $p>0.1$), ($\beta=-0.033$, $p<0.1$) and ($\beta=-0.048$, $p>0.01$).

6.13.1.2. Board of Director's Characteristics and ROA

The outcome of multivariate regression analysis between the board of director's characteristics (board size, board independence, board meeting, board change, secretary role, legal counsel and foreign member on the board) and firm performance (ROA) with corresponding coefficient value and t-value are presented in Table 6.20. The results indicate that the relationship between board size (BOARDSIZE) and ROA is negative, but not significant ($\beta=-0.000$, $p>0.1$). Thus, this result does not support hypothesis H1a. Moreover, the outcomes show that there is a negative association between the board independence (BORADIN) and ROA, but not significant ($\beta=-0.015$, $p>0.1$). Therefore, this outcome does not support hypothesis H2a. Similarly, with consistent to the board meeting (BOARDME) was found to be insignificant predictor of the ROA ($\beta=-0.002$, $p>0.1$), Thus, this finding does not support hypothesis H3a. The Table 6.20 also presents a negative however, not a significant relationship between the board change (BOARDCH) and ROA ($\beta= -0.002$, $p>0.1$). Hence, this result does not support hypothesis H4a.

Moreover, the Table 6.20 shows that the secretary role has a negative significant relationship with ROA ($\beta= -.029$, $p<0.05$). Thus, this outcome supported hypothesis H5a. In addition, Table 6.20 provides that there is positive relationship between the legal counsel (LEGALCO) and ROA, but not significant ($\beta=0.018$, $p>0.1$). Thus, this outcome does not support hypothesis H6a. Finally, for the foreign member (BOFOREIGN), there

is a positive relationship between foreign member (BOFOREIGN) and ROA, but not significant ($\beta = 0.031$, $p > 0.1$). Therefore, this result does not support hypothesis H7a.

6.13.1.3 Audit Committee Characteristics and ROA

In this section, this study discusses the relationships between three variables related to the audit committee characteristics, namely size, independence and meeting and the ROA. Table 6.20 reveals that all the three characteristics of audit committee are not significantly associated with ROA. These findings do not support the hypotheses H8a, H9a, and H10a. However, the results show that there is positive relationship between the audit committee size (ACSIZE) and ROA, but not significant ($\beta = 0.006$, $p > 0.1$). Moreover, the same results are displayed by the audit committee independence (ACINDE) that there is no significant relationship exist between the audit committee independence (ACINDE) and ROA ($\beta = 0.032$, $p > 0.1$). Finally, the audit committee meeting has a positive, but not a significant relationship with ROA ($\beta = 0.007$, $p > 0.1$).

6.13.1.4 Executive Committee and ROA

Table 6.20 reveals that the executive committee's existence (ECEX) is not significantly associated with ROA ($\beta = -0.019$, $p > 0.1$). Thus, this outcome does not support hypothesis H11a.

Table 6.20
Summary of the Hypotheses Related to ROA

Hy no	Variables	Expected signs	Coef	P>	Decision
H1a	Board Size (BOARDSIZE)	+/-	-.000	0.919	Not Supported
H2a	Board independence (BORADINDE)	+	-.015	0.767	Not Supported
H3a	Board Meeting (BOARDME)	+/-	-.002	0.58	Not Supported
H4a	Board Change (BOARDCH)	+/-	-.002	0.852	Not Supported
H5a	Secretary (SECRETA)	+/-	-.029	0.034**	Supported
H6a	Legal Counsel (LEGALCO)	+/-	.018	0.179	Not Supported
H7a	Foreign Member (BOFOREIGN)	+/-	0.031	0.396	Not Supported
H8a	Audit Committee Size (ACSIZE)	+/-	.006	0.636	Not Supported
H9a	Audit Committee Independence (ACINDE)	+	.032	0.516	Not Supported
H10a	Audit Committee Meeting (ACMEETIN)	+	.007	0.223	Not Supported
H11a	Executive Committee Existence (ECEX)	+/-	-.019	0.257	Not Supported
	FIRM SIZE (FIRMSIZE)	+/-	.009	0.199	
	Leverage (LEVERAG)	+	-.188	0.000***	
	Industry (INDUSTRY)	+/-	.006	0.766	
	2009	+/-	-0.004	0.819	
	2010	+/-	0.029	0.11	
	2011	+/-	-0.033	0.072*	
	2012	+/-	-0.048	0.709	

Notes:

*** Correlation is significant at the 0.01 level (2- tailed).

** Correlation is significant at the 0.05 level (2- tailed).

* Correlation is significant at the 0.1 level (2- tailed).

6.13.2 Model (2) and Result of Analysis

In this section, the results of the analysis of the relationship between firm performance (Tobin-Q) (dependent variable) and board of directors' characteristics (board size, board independence, board meeting, board change, secretary role, legal counsel and foreign

member on the board), audit committee characteristics (size, independence and meeting), executive committee and firm size, leverage, industry and time period (a control variable) are presented through multivariate regression analysis.

6.13.2.1 Control Variables and Tobin-Q

Four control variables have been included in the present study, namely firm size, debt, industry and years. The first control variable was the firm size. The use of firm size as the control variable is justified by the findings of companies with various distinct characteristics. In this context, Patro, Lehn and Zhao (2003) highlighted the possibility of firm size and growth being significant determinants of the size and the structure of the board. Additionally, the firm size affects its performance and is generally used as a control variable in empirical studies dedicated to corporate governance (e.g. Andres *et al.*, 2005; Ghosh, 2006; & Yan *et al.*, 2007). The impact of firm size upon corporate governance is clear from the findings that indicate larger companies to be less effective in comparison to their smaller counterparts, because even though the former follows government bureaucracy, they contain more ambiguity and are riddled with agency issues (Patro *et al.*, 2003). Based on the results depicted in Table 6.21, there is a negative relationship between firm size (FIRMSIZE) and Tobin-Q but it is statistically insignificant ($\beta=0.009$, $p>0.1$).

Second control variable was leverage that can be described as the total sum of long-term debt and short-term/extended liability as a percentage of total assets. Moreover, debt ratio

impacts the outcomes of the company. A positive effect may result in the minimised cash flow, and company control which reveals more of the market. According to the results in Table 6.21, there is a negative relationship between leverage (LEVERAG) and Tobin-Q and this relationship is not significant ($\beta=-0.080$, $p>0.1$).

Third, regarding the industry sector as a control variable in the model, Hoppenstedt (1999) shed a light on the industry sectors and the average number of employees for every company. To indicate the industry codes, a dummy variable was employed to represent manufacturing versus non-manufacturing firms. In prior studies, such as Core, Holthausen and Larcker (1999), Gillan, Hartzell and Starks (2003) and Core, Guay and Rusticus (2005), firm performance determinants include industry performance, return volatility, opportunities for growth and firm size. The Table 6.20 reveals that the industry sector was found to be insignificant to Tobin-Q ($\beta=.006$, $p>0.1$).

The fourth control variable was the Time Period. According to the results presented in Table 6.21, the performance over the years is similar with the exception of 2010 that displays a negative significant performance. This may be attributed to the unstable conditions in the Middle East that drove many investors to transfer their economic activities to other stable countries. This held true even for Oman. It is a general assumption that investors invest their money in an environment characterised by safety where they can wait for short term profits rather than a long term one. Based on Table 6.21, the companies' performance failed to show significance throughout the years,

except in 2010 when Tobin-Q was positively and significantly affected (2009, 2010, 2011 and 2012) ($\beta=0.065$, $p>0.1$), ($\beta=0.114$, $p>0.05$), ($\beta=0.012$, $p>0.1$) and ($\beta=-0.002$, $p>0.1$).

6.13.2.2 Relationship between Board of Directors' Characteristics, Audit Committee Characteristics, Executive Committee and Tobin-Q

6.13.2.2.1 Board of Director's Characteristics and Tobin-Q

The outcome of multivariate regression analysis between the board of director's characteristics (board size, board independence, board meeting, board change, secretary role, legal counsel and foreign member on the board) and firm performance (Tobin-Q) with corresponding coefficient value and t-value is presented in Table 6.21. The results indicate that the relationship between board size (BOARDSIZE) and ROA is strongly positive and significant ($\beta=0.067$, $p<0.05$) supporting hypothesis H1b. Similarly, board meeting (BOARDME) has a positive and significant relationship with Tobin-Q ($\beta=0.030$, $p<0.05$). So, this outcome supports hypothesis H3b. On contrary, Table 6.21 shows that the board independence (BORADIN) has a negative, but not significant effect on Tobin-Q ($\beta=-0.352$, $p>0.1$) thus, this result does not support hypothesis H2b.

According to the same findings, the results in Table 6.21 indicate that there is no significant relationship between the board change (BOARDCH) and Tobin-Q ($\beta=0.034$, $p>0.1$). Thus, H4a is not supported. Furthermore, the association between the secretary role (SECRETAR) and Tobin-Q is found to be insignificant ($\beta=0.001$, $p>0.1$) that is not supporting the hypothesis H5b. In addition, as evident from Table 6.12, there is a positive yet not significant relationship between legal counsel (LEGALCO) and Tobin-Q

($\beta=0.008$, $p>0.1$) which is not in favour of the hypothesis H6b. Finally, the foreign member (BOFOREIGN) has a negative, but not a significant relationship with Tobin-Q ($\beta=-0.216$, $p>0.1$) which is not in line with hypothesis H7b.

6.13.2.2.2 Audit Committee Characteristics and Tobin-Q

Moreover, the present study provides three variables related to audit committee characteristics, namely size, independence and meeting. Table 6.21 reveals that one out of three characteristics of the audit committee is significantly associated with Tobin-Q. The results show that there is a negative relationship between the audit committee size (ACSIZE) and Tobin-Q, but not significant ($\beta= -0.030$, $p>0.1$) which is not favouring hypothesis H8b. On the other hand, the audit committee independence (ACINDE) has a positive yet not significant relationship with Tobin-Q ($\beta=0.1301$, $p>0.1$). Thus, this result does not support hypothesis H9b.

Furthermore, the same results are revealed for the audit committee meeting; a negatively significant relationship was found between the audit committee meeting (ACMEETIN) and Tobin-Q ($\beta=-0.062$, $p<0.05$). Therefore, this finding supports hypothesis H10b.

6.8.2.2.3 Executive Committee and Tobin-Q

Table 6.21 provides a negative significant relationship between the executive committee (ECEX) and Tobin-Q ($\beta=-0.109$, $p<0.1$). Consequently, this outcome is supporting hypothesis H11b.

Table 6.21
Summary of the Hypotheses Related to Tobin-Q

Hy no	Variables	Expected signs	Coef	P>	Decision
H1b	Board Size (BOARDSIZE)	+/-	0.067	0.022**	Supported
H2b	Board independence (BORADINDE)	+	-0.352	0.205	Not Supported
H3b	Board Meeting (BOARDME)	+/-	0.030	0.012**	Supported
H4b	Board Change (BOARDCH)	+/-	0.034	0.379	Not Supported
H5b	Secretary (SECRETA)	+/-	0.001	0.986	Supported
H6b	Legal Counsel (LEGALCO)	+/-	0.008	0.840	Not Supported
H7b	Foreign Member (BOFOREIGN)	+/-	-0.216	0.135	Not Supported
H8b	Audit Committee Size (ACSIZE)	+/-	-0.030	0.386	Not Supported
H9b	Audit Committee Independence (ACINDE)	+	0.1301	0.561	Not Supported
H10b	Audit Committee Meeting (ACMEETIN)	+	-0.062	0.003***	Supported
H11b	Executive Committee Existence (ECEX)	+/-	-0.109	0.052*	Supported
	FIRM SIZE (FIRMSIZE)	+/-	0.009	0.757	Not Supported
	Leverage (LEVERAG)	+	-0.080	0.563	Supported
	Industry (INDUSTRY)	+/-	-0.0876	0.486	Not Supported
	2009	+/-	0.065	0.176	
	2010	+/-	0.114	0.026**	
	2011	+/-	0.012	0.856	
	2012	+/-	-0.002	0.966	

Notes: *** > 0.01, ** > 0.05, * > 0.1.

6.14 Summary of Hypotheses Testing: Corporate Governance and Firm Performance

The findings extracted from Pearson correlation analysis and multivariate regression are provided in this chapter. Table 6.22 presents the summaries of the findings associated to the hypotheses testing techniques at three levels of significance; 0.01, 0.5 and 0.1. The analysis displays the influence of the board of directors' characteristics, audit committee characteristics and executive committee on firm performance (ROA and Tobin-Q) and presents conflicting results.

With reference to the findings, board size has a negative, but an insignificant relationship with ROA. On the other hand, the association between board size and Tobin-Q is positively significant. Thus, this finding does not fully support the hypothesis. Moreover, board independence has a negative relationship with ROA or Tobin-Q but not significant. Therefore, this result does not fully support the hypothesis.

In addition, board meeting does not have a significant relationship with ROA, but it has a positive significant relationship with Tobin-Q indicating partial support of the relationship. Moreover, board change, the legal counsel and foreign member on the board are not significantly related with both ROA and Tobin-Q. Thus, this result does not fully support the hypothesis.

Secretary role has a significant negative relationship with ROA and it has a positive association with Tobin-Q but not significant. Consequently, this result partially supports the hypothesis. On the other hand, the relationship between audit committee size and committee independence is not significant with both ROA and Tobin-Q. Hence, this result does not support the hypothesis. Finally, the audit committee independence and executive committee existence are not significantly related with ROA, but they are positively and significantly related with Tobin-Q. Hence, this result partially supports the hypothesis.

Table 6.22
Summary of the Hypotheses Testing Results

Hy no	Hypothesis statement	Decision
H1	There is a relationship between board size and firm performance.	Partially Supported
H2	There is a positive relationship between board independence and firm performance.	Not Supported
H3	There is a relationship between the number board meeting and firm performance.	Partially Supported
H4	There is a relationship between the board change and firm performance.	Not Supported
H5	There is a relationship between the role of secretary on the board and firm performance.	Partially Supported
H6	There is a relationship between the legal counsel and firm performance.	Partially Supported
H7	There is a relationship between foreign member on the board and firm performance.	Not Supported
H8	There is a relationship between audit committee size and firm performance.	Not Supported
H9	There is a positive relationship between audit committee independence and firm performance.	Not Supported
H10	There is a relationship between audit committee meeting and firm performance.	Partially Supported
H11	There is a relationship between the executive existence and firm performance.	Partially Supported

In summary, the study results obtained from Pearson correlation and multivariate regression analysis showed that some hypotheses were supported while others were not. Specifically, Table 6.22 indicates that H1, H3, H5, H10 and H11 were partially supported. On the other hand, H2, H4, H6, H7, H8 and H9 were not supported.

6.16 Summary of the Chapter

This chapter offers the analysis of the response rate, the descriptive analysis of the variables and Pearson correlation analysis. This was followed by the discussion of detecting outliers and also the testing of assumptions which are namely, normality, multicollinearity, linearity, heteroscedasticity, contemporaneous correlation, autocorrelation and independence of the error terms prior to conducting the regression analysis. Moreover, all these tests were conducted to test the stability and the robustness of the findings for Tobin-Q. The result are summarised in Table 6.13 and Table 6.22. Finally, the next chapter discusses the findings, conclusions, implications, limitations as well as suggestions for future research of the study.

CHAPTER SEVEN

DISCUSSION AND CONCLUSION

7.1 Introduction

This chapter is dedicated to discuss the findings obtained from the results presented in Chapter Six. It comprises of six sections: first, the study summary is presented in section 7.2 and this is followed by a detailed discussion of the hypotheses in section 7.3. Section 7.4 contains the study's implications and Section 7.5 addresses the study limitations and recommendations for future study. The findings of the study are reported in section 7.6.

7.2 Summary of the Study

This study was motivated by the issues arising from the conflict of interests existing between shareholders and management within the corporate governance structure system. This may influence the quality of Omani companies' performance. Hence, to keep this conflict of interest under control and to minimise the agency costs, several internal and external tools, namely CG mechanisms have been recommended. For instance, board of director's characteristics, audit committee characteristics, executive committee and board diversity is established as a solution for such conflicts.

More specifically, the motivations of this study can be reported as follows: Firstly, the majority of the prior studies focused on the relationship between CG and firm performance in the developed countries while developing economies, like Oman, were

overlooked. It is also widely acknowledged that only few studies investigated the board of directors independence in general, and in the Gulf countries in particular (in the context of Oman's legal system) and their impact upon the firms' practices (Al-Hussain & Johnson, 2009; Aljifri & Moustafa, 2007; Al-Matari *et al.*, 2012; Al-Matari *et al.*, 2012a; Al-Matari *et al.*, 2012b; Ghabayen, 2012; Najjar, 2012).

Secondly, in the context of Oman's Stock Exchange, the MSM currently experienced a crash, which resulted in CMA suspending the trading of two firms (National Rice Mills (SAOG), and Oman National Company Holding (SAOG)). These have led to the issues concerning the effectiveness of various monitoring mechanisms that were set up to protect the interests of investors in the country (Dry, 2003). The possibility that the collapse of the two companies is due to the non-application of the principles of corporate governance, which regulates the management of the company and helps to separate the terms of reference and functions. This is also due to (as it is the case of some companies), the fact that some of the people are under the leadership of the royal. Therefore, the collapse of the companies can be argued to be due to the lack of commitment in applying the CG.

Thirdly, the CMA issued the CG regulations in 2002, in response to the criticisms to the Omani corporate management just after the crash in 1997. Nevertheless, the Omani CG is still in its infancy stage and the CMA is expanding efforts to educate the market about the benefits of the application of an effective CG mechanism (World Bank, 2009). Moreover, according to the reports, several regulations have just been established without testing

them and this has led to the least awareness of effective CG and practices that remained in their initial stages.

Fourthly, studies concerning CG in GCC are still limited such as Al-Hussain and Johnson (2009) in Saudi Arabia, Aljifri and Moustafa (2007) in the UAE, Al-Matari *et al.* (2012a, 2012b) in Saudi Arabia, Al-Matari *et al.* (2012a and b) in Kuwait, Al-Najjar (2013) in five middle east countries, Ghabayen (2012) in Saudi Arabia and Najjar (2012) in Bahrain. In the context of Oman, the CG-firm performance relationship has been greatly overlooked in the previous studies. Furthermore, the study concerning the relationship between the board of directors' characteristics (board size, board independence, board meeting, board change, secretary role, legal counsel and foreign member on the board), audit committee characteristics (size, independence and meeting), executive committee and their effects on firm performance is still lacking in the CG literature (Al-Matari *et al.*, 2012; Al-Matari *et al.*, 2012a, 2012b).

Fifthly, Oman is the pioneering GCC country to apply the Code of Corporate Governance that was established in 2002. It is also the sole GCC country that is not a member of OPEC. This decision was taken to encourage the oil market to review its economy at any time. As a result, recent oil prices supported Oman's budget, trade surpluses, and foreign reserves. The heightened expenditures in 2011 during Oman's Arab Spring (around OMR 1 billion, or \$2.6 billion) counteracted increased oil revenues while the significant oil prices assisted in steering clear of budgetary deficits. A thorough review of the literature related to the relationship between CG and firm performance reveals that the findings are

inconclusive. Specifically, the findings of empirical studies carried out in the US, UK, Chile, Hong Kong and other countries regarding firms' performance were found to be inconsistent. Moreover, there is still a lack of studies to explore this relationship in Oman. Moreover, this study is one of the few studies in the gulf countries in general (Al-Hussain & Johnson, 2009; Aljifri & Moustafa, 2007; Al-Matari *et al.*, 2012; Al-Matari *et al.*, 2012a; Al-Matari *et al.*, 2012b; Al-Najjar, 2013; Ghabayen, 2012; Najjar, 2012) and in Oman in particular to explore the CG and firm performance relationship (Al-Matari *et al.*, 2012).

Additionally, earlier literature highlighted that a little attention was paid to examine the relationship between variables related to board of directors' characteristics (board change, secretary role, legal counsel and foreign member on the board) and firm performance (Al-Matari *et al.*, 2012). Prior studies were limited to examine the impact of the board of directors' characteristics (board size, board independence and board meetings) upon the performance of the firm (e.g. Chaghadari, 2011; Chidambaran, Palia & Zheng, 2009; Hsu & Petchsakulwong, 2010; Ibrahim & AbdulSamad, 2011; Jackling & Johl, 2009; Kang & Kim, 2011; Khan & Javid, 2011; Kota & Tomar, 2010; Lin, 2011; Nanka-Bruce, 2011; Nuryanah & Islam, 2011; Rachdi & Ameer, 2011; Rahmat, Iskandar & Saleh, 2009; Reddy *et al.*, 2010; Saibaba & Ansari, 2011; Shah, Javed & Abbas, 2009; Siala, Adjaoud & Mamoghli, 2009; Yasser, Entebang & Mansor, 2011).

Likewise, there has also been little attention paid to the relationship between the characteristics of the audit committee and the performance of the firm (Black & Kim,

2007; Black *et al.*, 2003; Heenetigala & Armstrong, 2011; Kyereboah-Coleman, 2007; Obiyo & Lenee, 2011; Swamy, 2011). Inconsistent with the essential role of this committee in enhancing firm performance (Forker, 1992; Kim & Yoon, 2007; Saibaba & Ansari, 2011) and as suggested by other researchers (Al-Matari *et al.*, 2012; Hsu & Petchsakulwong, 2010; Mollah & Talukdar, 2007), the committee's characteristics are examined in light of the CG.

Most importantly, there is a lack of studies dedicated to the association between the executive committee and firm performance (ROA and Tobin-Q). Previous studies just focused on the relationship between the board of directors with audit committees and firm performance (Abdurrouf, 2011; Al Manaseer *et al.*, 2012; Li *et al.*, 2012; Kang & Kim, 2011; Nanka-Bruce, 2011; Obiyo & Lenee, 2011; Yasser, Entebang & Mansor, 2011). Theoretically, this study highlights the agency theory, resource dependence theory and CG perspective in relation to firm's performance. Few studies, like Bektas and Kaymak (2009), Douma *et al.* (2006), Kyereboah-Coleman (2007), Lawal (2012), Lin (2011) and Major and Marques (2009) only discussed the importance of resource dependence theory in relation to the firm's performance. Furthermore, this study demonstrates that the resource dependence theory complements the other theories, namely the agency theory. These theories are suggested to be employed by Al-Matari *et al.* (2012) to examine the relationship between CG and firm performance.

To contribute in bridging the gaps in the literature, the primary objective of this study is to examine the relationship between CG mechanisms, namely board of directors'

characteristics (board size, board independence, board meeting, board change, secretary role, legal counsel and foreign member on the board), audit committee characteristics (size, independence and meeting), executive committee and firm performance (ROA and Tobin-Q) of the public listed companies in Omani MSM.

On the basis of the problems which have been explained in the previous chapters and the literature review presented in Chapter One, Chapter Two and Chapter Three, this study aimed to achieve the following central objectives:

1. To examine the association between the board of directors' characteristics (board size, board independence, board meeting, board change, secretary role, legal counsel and foreign member on the board) and firm performance (ROA and Tobin-Q).
2. To investigate the relationship between audit committee characteristics, namely, size, independence, meeting and firm performance (ROA and Tobin-Q).
3. To explore the association between the executive committee and firm performance (ROA and Tobin-Q).

In an attempt to achieve the aforementioned objectives, an extensive literature review was conducted and discussed throughout the study. The framework of the study was developed based on the agency and the resource dependence theories in the light of the internal CG mechanisms and firm performance.

To examine the proposed model, the data for the years 2008 through 2012 was collected from MSM. Specifically, secondary data was gathered from annual reports of all non-financial companies listed on the MSM for five years 2008, 2009, 2010, 2011 and 2012. The study sample comprised of 78 non-financial firms (390 observations). Then, this data was run, using multivariate regression analysis, to test the hypothesis regarding the relationship between CG variables (board of director's characteristics, audit committee variables and executive committee) and firm performance. The firm performance was measured using two measurements, namely ROA and Tobin-Q, which were deemed as respective proxies for market measurement and accounting measurement.

Specifically, to achieve the study objectives, three sets of hypotheses were developed. The first set of the hypotheses were to examine the relationship between the board of director's characteristics (board size, board independence, board meeting, board change, secretary role, legal counsel and foreign member on the board variables) and firm performance (ROA and Tobin-Q). The second sets of hypotheses were established to capture the relationship between audit committee characteristics (size, independence and meeting), variables and firm performance (ROA and Tobin-Q). The third sets of hypotheses were to investigate the association between the executive committee and firm performance (ROA and Tobin-Q). Based on the analysis results, the impact of CG mechanisms variables upon ROA and Tobin-Q is dissimilar.

With regards to the board of director's characteristics, no relationship was found to be significant between board size and ROA while, a positive significant association was

found between board size and Tobin-Q. The board of director's independence variable was found to be a negative and insignificant predictor of performance based on both measures of firm performance (ROA and Tobin-Q). Whereas board meeting variable was reported not to be significantly related to ROA, but a positive significant relationship was found between the board meeting and Tobin-Q. The board change was reported to be insignificantly related to both measures of firm performance (ROA and Tobin-Q). In the same path, the relationship between the roles of secretary on the board was reported to be negatively significant to ROA, however, it was found to be insignificant to Tobin-Q. The legal counsel variable was as well found to be insignificantly related to both ROA and Tobin-Q. Finally, the foreign member on the board was also found to be insignificant to both ROA and Tobin-Q.

For audit committee characteristics, the audit committee size was found to be insignificantly related to both measurements of firm performance (ROA and Tobin-Q). Along the same line, the audit committee independence variable was found to be insignificantly related to both ROA and Tobin-Q. The audit committee meeting was revealed to be insignificantly linked to ROA but it was found to be negative significant to Tobin-Q. For executive committee, the executive committee's existence was reported to have no significant relation to ROA, but it was negatively significant to Tobin-Q. Eventually, the outcomes are considered to be of significance for academicians, practitioners, policy makers and others concerns as discussed in the following sections. Moreover, the limitations of the study the future research are further discussed in details.

7.3 Discussion of Hypotheses

Table 7.1
Summary of the All Findings

Hy No	Variables	ROA		TobinQ	
		Coef	P>	Coef	P>
1	Board Size (BOARDSIZE)	-.000	0.919	0.067	0.022**
2	Board independence (BORADINDE)	-.015	0.767	-0.352	0.205
3	Board Meeting (BOARDME)	-.002	0.58	0.030	0.012**
4	Board Change (BOARDCH)	-.002	0.852	0.034	0.379
5	Secretary (SECRETA)	-.029	0.034**	0.001	0.986
6	Legal Counsel (LEGALCO)	.018	0.179	0.008	0.840
7	Foreign Member (BOFOREIGN)	0.031	0.396	-0.216	0.135
8	Audit Committee Size (ACSIZE)	.006	0.636	-0.030	0.386
9	Audit Committee Independence (ACINDE)	.032	0.516	0.1301	0.561
10	Audit Committee Meeting (ACMEETIN)	.007	0.223	-0.062	0.003***
11	Executive Committee Existence (ECEX)	-.019	0.257	-0.109	0.052*

Notes:

*** Correlation is significant at the 0.01 level (2- tailed).

** Correlation is significant at the 0.05 level (2- tailed).

* Correlation is significant at the 0.1 level (2- tailed).

Based on the findings and results reported, Table 7.1 summarised the major findings regarding the hypotheses of the study. The proceeding sections provide discussions on the findings generated by the two models in light of accounting-based measurement (ROA) and the marketing-based measurement (Tobin-Q).

7.3.1 Discussion of First Model (Results Based on Accounting Measure)

In this section, this current study provided the hypothesis testing of board of directors' characteristics (board size, board independence, board meeting, board change, secretary role, legal counsel and foreign member on the board), audit committee characteristics (size, independence and meeting) and executive committee and the firm performance (ROA). As consistent with the results in Table 7.1, some of the variables were found to be associated with ROA.

7.3.1.1 Board of Director's Characteristics

7.3.1.1.1 Board Size and ROA

Contrary to the agency theory and resource dependence theory prediction, the relationship between the board size and ROA was found to be negatively insignificant indicating that the hypothesis H1a is not supported. The result shows that board size does not contribute in improving the firm performance. This finding is not in line with the Code of Corporate Governance in Oman (2002) that recommended all listed companies to choose the members of the board because their role is very essential in overseeing all the company operations and to make the right decision to maximise the wealth of the company members. This is due to the fact that the board of directors is a primary mechanism which controls and monitors management behaviour.

The results obtained in this study are in line with some earlier studies, that reported no relationship between the board size and ROA whether in the developed countries such Bhagat and Bolton (2008), Millet-Reyes and Zhao (2010), Reddy, Locke and Scrimgeour (2010), Shao (2010) and Wei (2007) or in the developing countries like Abdurrouf (2011), Al-Matari *et al.* (2012), Bektas and Kaymak (2009), Chiang and Lin (2011), Ghabayen (2012), Ibrahim and Abdul Samad (2011), Kamardin (2009), Ibrahim *et al.* (2010), Kyereboah-Coleman (2007), Chaghadari (2011), Noor (2011), Latief, Raza and Gillani (2014), Prabowo and Simpson (2011) and Rachdi and Ameer (2011) and Vo and Nguyen (2014).

However, this finding is in contrast to previous researchers who found a negative relationship between the board size and ROA whether in the developed countries ((Irina & Nadezhda, 2009; Juras & Hinson, 2008; O'Connell & Cramer, 2010) or the developing nations (Mashayekhi & Bazazb, 2008; MoIlah & Talukdar, 2007; Haniffa & Hudaib, 2006). It is also against prior authors who reported a negative association between the board size and ROA whether in the developed countries such as Bauer *et al.* (2009), Larmou and Vafeas (2010) and Premuroso and Bhattacharya (2007) or in the developing countries such as Abdullah *et al.* (2008), Chahine and Safieddine (2011), Chugh *et al.* (2011), Chung *et al.* (2008), Ehikioya (2009), Jackling and Johl (2009), Kyereboah-Coleman and Biekpe (2006) and Swamy (2011).

The non-significant effect of board size on ROA can be discussed in the light of the following plausible justifications:

Firstly, a large board size does not translate the fact that a majority of board members represents the stakeholders' interests (Shao, 2010) and in the same manner, the board size does not reflect its effectiveness. A board with sufficient experience and knowledge should ensure board effectiveness (Shakir, 2008). Therefore, the association between board size and firm performance may differ owing to the differences in the characteristics of national institutions and the firm's specific characteristics (Guest, 2009). Stated differently, the board's functions are different because of their different institutional backgrounds. Hence, the expected relationship between board size and firm performance could be dissimilar.

Secondly, the possibility that CEO dominates the board activities which form information asymmetry. This means that the CEO may confine the board from performing an effective monitoring role (Kamardin, 2009).

Thirdly, the high concentration of ownership in public listed companies in Oman and the prevalence of cross-holdings of share ownership may have an influence. The issue of ownership concentration in Omani companies is the dominance of large shareholders, exercising control rights and may attempt to expropriate the assets of the company to the detriment of the minority shareholders' rights. Hence, in Oman, safeguarding minority shareholders' rights remains a primary issue as controlling shareholders dominate through ownership concentration and representation of company board and management.

Finally, the issues of free-riding and relative challenge in building consensus (Kyereboah-Coleman, 2007) may be behind the findings. Hence, it may be stated that these issues behind the justification could be unique to the Omani system.

7.3.1.1.2 Board Independence and ROA

While previous studies suggested that there is a positive relationship between the board independence and ROA, this study, as depicted in Table 7.1 found a negative insignificant link between the board independence and ROA.

Board independence is another essential variable in the board of director's characteristics that may improve the performance of the companies. The agency theory indicates that sufficient monitoring mechanisms should be laid down to safeguard shareholders from management's selfish behaviours. Thus, the majority of external directors on the board is considered to have a positive effect on performance (Fama & Jensen, 1983; Jensen & Meckling, 1976; Shleifer & Vishny, 1997). In line with the resource dependence theory, the external sources provide a firm with external channel to improve the performance of the company. Moreover, an independent board allows board members to comprehend complex environments and give multiple knowledge and experience from different sources, and in turn improves firm performance (Pfeffer, 1972). In consistent with both theories and the Code of the Corporate Governance, whether in the Oman or in other countries, the board independence enhances the performance of the companies.

This finding is similar with some previous studies, that were conducted in some developed countries like Adjaoud *et al.* (2007), Belkhir (2005), Bøhren and Strøm (2010), García-Sánchez (2010) , Hu *et al.* (2010), Siala *et al.* (2009), Wei (2007) and Yue *et al.* (2008) and in the developing countries such as, Al-Matari *et al.* (2012), Chowdhury (2010), Chugh *et al.* (2011), Guoa and KGAb (2012), Ibrahim and Abdul Samad (2011), Ibrahim *et al.* (2010), Kaur, 2014; Kota and Tomar (2010), Kumar and Singh (2012), Chaghadari (2011), Latief, Raza and Gillani, 2014; Noor (2011), Ghazali (2010), Pandya (2011), Prabowo and Simpson (2011), Rachdi and Ameer (2011) and Sahu and Manna (2013).

However, this finding is in contrast to previous researchers who found a positive significant relationship between the board independence and ROA in the developed countries (Bhagat & Bolton, 2009; Chamberlain, 2010; Dey, 2008; Filatotchev *et al.*, 2007; Harjoto & Jo, 2008; Heenetigala & Armstrong, 2011; Juras & Hinson, 2008; O'Connell & Cramer, 2010; Premuroso & Bhattacharya, 2007; Reddy *et al.*, 2010) and in the developing countries (Abdurrouf, 2011; Al Manaseer *et al.*, 2012; Azam *et al.*, 2011; Chiang & Lin, 2011; Cho & Kim, 2007; Filatotchev, Lien & Piesse, 2005; Ibrahim & Abdul Samad, 2011; Kamardin, 2009; Hsu, Hsiao, Li , 2009; Jackling & Johl, 2009; Khan *et al.*, 2011; Kyereboah-Coleman & Biekpe, 2006; Kyereboah-Coleman, 2007; Mashayekhi & Bazazb, 2008; Swamy, 2011).

Moreover, this result is not in line with the global and the Omani Code of Corporate Governance (2002), which suggested that the board must have a majority of independent

members as the independent directors are primarily responsible to monitor and control firm activities effectively in order to lessen management's opportunistic behaviour and expropriation of firm resources.

One possible explanation of the insignificant relationship between board independence and ROA is the major actions adopted by the board. The non-relationship between the outside directors share and company performance would support signalling theory. Owing to the poor company performance, outside directors are appointed by management or controlling shareholders to enhance performance with the professional competencies of directors and to relay a positive signal to the firm investors (high outside directors share is deemed as the best corporate governance practices) (Irina & Nadezhda, 2009; Firth *et al.*, 2006).

The second plausible explanation behind the insignificant relationship between board independence and ROA lies in the fact that outside directors may negatively affect the companies' performance because of lack of competence or motivation. This is evident in the practice of Omani companies; when firms experience bad performance the companies invite outside directors to their supervisory boards, to relay a positive signal to firm investors. If most board members are also insiders, the company positively experiences quick decision making by individuals possessing authentic knowledge of the organisation and financial industry.

The third explanation regarding the insignificant association between board independence and ROA is the caution against the negative relation between board independence and future operating performance. If the aim of board independence is to enhance performance, such exerted efforts may be misguided. On the other hand, if the aim of board independence is to oversee the poor performance of firms, then this may be justified. Finally, although good governance indices are positively linked to future operating performance, both policy makers and corporate boards should be careful in their emphasis on the indices components as they may worsen the issue of management entrenchment, particularly in situations where management requires disciplining (in negatively performing firms) (Bhagat & Bolton, 2008).

7.3.1.1.3 Board Meeting and ROA

The other important factor of the board of director's characteristics is the board meeting. Agreeing with the agency theory and resource dependence theory, this study hypothesised a relationship between the board meeting and ROA. However, the finding as apparent in Table 7.1 revealed that board meeting has an insignificant relationship with ROA.

The board effectiveness is reflected through its meetings as, the more frequent the board meetings are, the more improved is expected to be the performance. On the other hand, the board of directors often increases the frequency of board meetings to solve issues concerning declining performance (Evans, Evans & Loh, 2002). Most often, routine tasks

occupy much of the board's meeting time and confine the chances for external directors to carry out meaningful control over management. It is also suggested that boards should be relatively inactive as poor performance is reflected by higher board activity (Jensen, 1993).

The result of the insignificant relationship between board meetings and ROA is similar to prior studies that found no association between board meetings and ROA such as Kyereboah-Coleman (2007) and Noor (2011).

However, this finding is in contrast to some previous studies that found a positive significant relationship between the board independence and ROA (Kamardin, 2009). Moreover, this finding is not in line with several preceding investigators who had found a negative significant connection between the board independence and ROA (Noor, 2011).

The first plausible justification of insignificant relationship between board meeting and ROA is that the board meeting is not necessarily a reflection of improved firm performance and more often than not, frequency of board meetings increases when problems arise (Jensen, 1993). In this context, Jackling and Johl (2009) contended that increased board meeting is a reaction to poor performance, which is in turn linked to enhanced operating performance in the future, highlighting the presence of a lag effect. Moreover, the board needs to balance the frequency costs and benefits (Khanchel, 2007).

Another viewpoint was provided by Rebeiz and Salame (2006) who stated that frequency of board meetings is secondary to its quality. In other words, frequent board meetings

means that the board is playing an erroneous operating role rather than an oversight one which is its actual role.

7.3.1.1.4 Board Change and ROA

This study hypothesised that the board change influences aspects of the firm, including strategy, policy and decision making. The finding as illustrated in Table 7.1 was not as expected.

The insignificant relationship between board change and ROA may be due to the poor recruiting policy when it comes to appointing certified persons. In other words, it could be attributed to the company's poor policy when it comes to selecting person in terms of education, experience, knowledge and others.

Therefore, it requires the appointment of competent people who are able to improve the performance of the company through their experiences and their close interaction with the market.

This finding can also be attributed to the strong control of chairman over the board who prevents others in the board to innovate and enhance the firm performance.

The insignificant relationship between board change and ROA may also be attributed to the variable's ambiguity in the Omani Code of Corporate Governance. This called for the establishment of board change every year. Government representatives in securities commission need to edit the Code of Corporate Governance, should add an article

stressing the importance of the change, and should make it mandatory. Government representatives in securities commission should encourage listed companies to employ obligations if these companies desire to change somebody in the board.

7.3.1.1.5 The Role of the Secretary on the Board and ROA

The role of secretary on the board is crucial because the secretary's primary role is to ensure that firm's business stays in the right direction. With regards to this study's hypothesis, there is a relationship between the role of secretary on the board and ROA. However, the finding as reported in Table 7.1 showed that there is a negative significant association between the role of secretary on the board and ROA. Therefore, H5a is not supported since this finding implies that the role of secretary is associated with lower performance.

The findings regarding the negatively significant relationship between the secretary of the board and ROA reveal that, this variable is probably not mandatory for all listed companies even though it is addressed in the Omani Code of Corporate Governance (2002) which could lead to poor results. As a result, the regulators must encourage all listed companies to understand the role of secretary of the board and provide clear insights.

By definition, it has a significant role in private as well as public companies in arranging efficient communication among sectors in order to achieve the firm's target and maximise shareholder's wealth. Nevertheless, no strict structure exists to ensure

compliance with the rules established by the security commission. Moreover, it is important for government representatives in the security commission to make it mandatory for all listed companies to adhere to the rules and update their Code of Corporate Governance to keep abreast with international codes. As a whole, there should exist cooperation between companies and security commission to encourage listed companies to amend policies and in turn performance.

7.3.1.1.6 Legal Counsel and ROA

The role of legal counsel in the firm is very essential to mitigate allegations of judicial matters. That is why this study hypothesised that the legal counsel may enhance the performance of the companies. The results in Table 7.1 were not in line with this expectation. This relationship was found to be insignificant and therefore, H6a was not supported.

To justify the non-significant relationship between legal counsel and ROA, it can be said that it is because of the possibility of the absence of limited policy in selecting professional legal counsel in the market to handle major problems and enhance the performance of the company. Therefore, the capital market authority must highlight the role of the legal counsel in firms.

This can be also attributed to the overlooking of this variable in the Omani Code of Corporate Governance and its importance in decreasing courts allegations and future contracts insurance. The variable generally decreases misunderstanding among

companies. Hence, owing to this novelty, the legal counsel is not given the deserved attention by the Omani Code of Corporate Governance. Moreover, there is also a lack of enforcement of all listed companies to employ the legal counsel for performance improvement and for maximisation of shareholder's wealth.

7.3.1.1.7 Foreign Member on the Board and ROA

This study expects that the number of foreign members of the board have a relationship with ROA. However, this result found that the number of foreign members of the board has an insignificant association with ROA as illustrated in Table 7.1.

The justification behind the insignificant relationship between the foreign members of the board and ROA may be attributed to the fact that the foreign members lack the knowledge on the domestic environmental and cultural issues in order to deal efficiently with the entire occurring situation and to make good decisions.

Another explanation is that the company may not provide enough opportunity for foreign members to familiarise themselves with firm information. It is important for the Omani security commission (OSC) to find out the conditions of foreign members' selection and their involvement in the firm activities and to provide them with the rights and duties needed to handle day-to-day work which may lead to an improved company performance. That is, companies should authorise the foreign members to involve themselves in the operations and the decision making process.

7.3.1.2 Audit Committee Characteristics

It is important to note that audit committee size, audit committee independence and the number of audit committee meetings presumably could continue to serve as corporate regulators to ensure management accountability and responsibility towards shareholders by ensuring that managers present true and fair view of the firms and avoid irregularities. Therefore, the committee size, independence and meeting of the audit committee characteristics are expected to serve as the blend of good CG structure in improving the firm's performance.

7.3.1.2.1 Audit Committee Size and ROA

Based on the agency theory and resource dependence theory, this study hypothesised that audit committee size is expected to enhance the ROA. This is so since the audit committee is primarily developed to help the BODs oversight function in an attempt to increase the financial disclosure. Moreover, the audit committee is one of the main elements of the CG system that plays a key role in monitoring the internal control framework effectiveness and overseeing and reviewing the process of financial reporting of a firm. It also acts as an intermediary among internal auditors, external auditors, managers and board of directors to establish a proper flow of information among them and to guarantee transparent reporting.

Based on the statistical results of the current study, there is an insignificant association between audit committee size and ROA as apparent in Table 7.1. Thus, hypothesis H8a is not supported.

This result is consistent with previous studies of Wei (2007) in China and Abdurrouf (2011), Ghabayen (2012), Kim and Yoon (2007) and Noor (2011) in developing countries.

However, this finding is not in line with those previous studies that found a negative relationship between audit committee size and ROA in developed countries such as Bozec (2005) and in developing countries like Mollah and Talukdar (2007).

Moreover, this result is not in line with some previous studies that found a positive relationship between audit committee size and ROA in developed countries (Bauer *et al.*, 2009; Premuroso & Bhattacharya, 2007; Reddy *et al.*, 2010) and in developing countries (Al-Matari *et al.*, 2012; Heenetigala & Armstrong, 2011; Kyereboah-Coleman, 2007; Obiyo & Lenee (2011; Swamy, 2011).

A possible reason for the finding of this study with regards to the relationship between the audit committee size and ROA is that audit committees in Oman are not considered as important as compared to the other countries. This result matches the insignificant result on audit committee size indicating that the role of some specific board practices aspects in developed countries of firm performance is absent in the case of Oman. Likewise the insignificant committee size and the insignificant results of the audit committee size

indicates that in a developing country like Oman; where the capital market is still developing, and the external corporate governance mechanisms are weak, the participants in the market deem independent boards to be more significant compared to board size or the audit committee's strength. Because external governance mechanisms are not as effective, board independence, reflected by the composition of independent commissioners and leadership structure, is opted in the Omani capital market.

Finally, some studies concentrated on AC effectiveness as opposed to size and do not view AC size as a significant factor in improving committee's effectiveness. To maintain effective AC, it should be comprised of independent experts and well-informed members and it should possess sufficient authority (Mohiuddin & Karbhari, 2010).

7.3.1.2.2 Audit Committee Independence and ROA

According to the agency theory and the resource dependence theory; the audit committee independence plays a key role in guaranteeing that CG practices of auditing are observing to effect financial report which leads to the increase of company performance. Therefore, this study hypothesised a positive association between audit committee independence and ROA. Based on the statistical results, this study found an insignificant relationship between audit committee independence and ROA, as apparent in Table 7.1. Consequently, H9a is not supported.

This result does not support the recommendation of Sarbanes-Oxley Act (2002), Cadbury Committee (1992) in the UK and the Omani Code of Corporate Governance (2002) that

the audit committee should have a majority of independent members in order to avoid conflict between managers and owners and in improving companies' performance. Moreover, this finding is not in line with previous studies that reported a positive association between audit committee independence and ROA in developed countries such as Dey (2008) and in developing countries like Abdullah *et al.* (2008) and Swamy (2011).

On the other hand, this result is consistent with the previous studies that found no association between audit committee independence and ROA in developing countries like Al-Matari *et al.* (2012); Ghabayen (2012), Kyereboah-Coleman (2007) and Noor (2011).

A conceivable explanation for this insignificant finding is that the sole existence of audit committee independence on the board may be insufficient for the audit committee to achieve its monitoring responsibilities to enhance firm's value. There should also be a large majority of expert-independent audit committee members serving on the audit committee to improve the value of the firm (Al-Matari *et al.*, 2013a).

Another possible reason is that it may be significant to appoint individuals with technical expertise and experience in order to guarantee value creation. Therefore, the Omani capital market authority must be a leading example for all listed companies to appoint persons with higher qualifications in order to improve long-term company plans.

A third possible reason is that, maybe the board independence members do not have a friendly relationship with all members of the board and hence cannot work with them as a team, make the right decision and achieve firm targets.

7.3.1.2.3 Audit Committee Meeting and ROA

In the light of the agency theory and the resource dependence theory, frequent meetings of the audit committee may lead to enhance financial accounting processes and superior performance. To examine this proposition, this study hypothesised that there is a relationship between audit committee meeting and ROA. However, the result as apparent in Table 7.1 shows that there is no significant association between them. Therefore, hypothesis 10a is not supported.

This result does not support the recommendations and guidelines provided by the Cadbury Committee (1992) in the UK, the BRC (1999) in the US and Omani Code of Corporate Governance (2002), that audit committee meeting should be held not less than three times yearly with a majority of independent directors. These meetings are important to solve the problems that may be faced during the life cycle of operations, which leads to improve firm performance.

This result is similar to the previous studies that were conducted by Al-Matari *et al.* (2012a+b), Kyereboah-Coleman (2007) and Noor (2011) and found an insignificant relationship between audit committee meeting and ROA.

Moreover, Rebeiz and Salame (2006) stated that meeting quality is what matters most and that the frequency does not always improve firm performance. Therefore, the frequency of audit committee meetings may maximise during financial distress or during controversial decisions involving, illegal or questionable activities.

Another possible explanation is that the frequency of audit committee meetings and ROA is that board meetings are not always useful as limited time Non-Executive Directors (NEDs) spend together is not spent on exchanging meaningful ideas among themselves and with management. This is generally acknowledged to naturally stem from the fact that setting the agenda for these meetings is conducted by chief executive officers.

7.3.1.3 Executive Committee and ROA

This study hypothesised that the executive committee has a relationship with ROA. However, the result was not according to the expectation as apparent in Table 7.1. Since this relationship was found to be insignificant.

The insignificant result between the executive committee and ROA may be due to the fact that executive committees are not considered as important as other committees in Oman. This result indicates that some specific board of director's practices of firm performance do not exist in Oman. The Executive committee is not taken into consideration along with its role and the value in Oman.

Another possible reason is due to the low presence of executive committee independence on the board which may not be sufficient for the executive committee to carry out its monitoring roles in order to better operate the firm. This should also be coupled with majority of expert-independent members of the committee to ensure the firm value.

A third reason for the insignificant result between executive committee independence and ROA could be the novelty of the committee and the lack of attention paid to it. It is imperative that the Omani capital market should update its Code of Corporate Governance in order to stay abreast with international changes. The Omani Security Commission (OSC) should also make it mandatory for listed companies to adhere to policy to improve performance.

Moreover, this insignificant result may be attributed to the appointment of individuals to the committee. Individuals with technical expertise and experience should be appointed to ensure creation of value. Hence, the authority of the Omani capital market must ensure that all listed companies should appoint persons of higher qualifications to improve achievement of long-term company plans. Eventually, the frequency of executive committee meetings variable has not been made mandatory for all listed companies which explain the downplaying of its significance.

7.3.2 Discussion of Second Model (Results Based on Marketing Measure)

In this section, the hypothesis statements were tested against Tobin-Q, such as board of directors' characteristics (board size, board independence, board meeting, board change, secretary role, legal counsel and foreign member on the board), audit committee characteristics (size, independence and meeting) and executive committee and firm performance (Tobin-Q) as evidenced from Table 7.1.

7.3.2.1 Board of the Director's Characteristics

7.3.2.1.1 Board Size and Tobin-Q

According to the agency theory and the resource dependence theory, this study hypothesised a relationship between board size and Tobin-Q. This relationship, as apparent in Table 7.1 is as expected since board size was found to be a positive and significant predictor of Tobin-Q. This finding suggests that larger boards are associated with higher performance and this supports the hypothesis H1b.

This finding is consistent with previous studies that found a positive relationship between board size and Tobin-Q whether in developed countries such as Albert-Roulhac and Breen (2005), Bauer *et al.* (2009), Danoshana and Ravivathani (2014), Khanchel (2007) and Lee (2009) or in developing countries like Abdullah *et al.* (2008), Black *et al.* (2003), Dwivedi and Jain (2005), Kamardin (2009), Jackling and Johl (2009), Kang and Kim (2011), Kyereboah-Coleman (2007), Haniffa and Hudaib (2006) and Sahu and Manna (2013). However, this finding is in conflict with previous studies that found a negative relationship between board size and Tobin-Q in the developed countries (Florackis, 2005; Irina and Nadezhda, 2009; O'Connell and Cramer, 2010) and in developing countries (Garg, 2007; Kota and Tomar, 2010; Amran and Che-Ahmad, 2009).

This finding is in line with the resource dependence theory, which postulates that the board has to be stricter, when it comes to monitoring the management, to ensure the minimal financial fraud. The benefits of having a bigger board may be counteracted by its

costs, as bigger boards face more challenges in achieving a consensus, which indicates that smaller boards could result in minimum coordination issues and improved efficient performance. The board should also contribute to valuable input to the manner in which strategic decisions are made in the firm.

Furthermore, the positive significant association between board size and Tobin-Q is due to the diverse experience possessed by the large number of directors. Therefore, bigger boards are more likely to possess the required knowledge and skills when compared to their smaller counterparts (Van & Levrau, 2004). Additionally, it is suggested that larger boards could decrease the authority of the CEO (Forbes & Milliken, 1999; Goodstein *et al.*, 1994) and thus the large board size enhances the company performance.

7.3.2.1.2 Board Independence and Tobin-Q

With regards to the relationship between board independence and Tobin-Q, the result of the study found a negative insignificant association, as apparent in Table 7.1. This result is not in line with global code and Omani Code of Corporate Governance that states that the board must have a majority of independent directors, as their primary role is to monitor and control firm activities in an effective manner to minimise managerial opportunistic behaviours and expropriation of firm resources.

This result is similar to earlier researches that found insignificant association between board independence and Tobin-Q whether in the developed countries such Bhagat and Bolton (2008), Millet-Reyes and Zhao (2010), Reddy, Locke and Scrimgeour (2010),

Shao (2010) and Wei (2007) or in the developing countries like Abdurrouf (2011), Al-Matari *et al.* (2012b), Bektas and Kaymak (2009), Chaghadari (2011), Chiang and Lin (2011), Ghabayen (2012), Ibrahim and Abdul Samad (2011), Ibrahim *et al.* (2010), Kamardin (2009), Kyereboah-Coleman (2007), Latief, Raza and Gillani (2014), Noor (2011), Prabowo and Simpson (2011), Rachdi and Ameer (2011) and Sahu and Manna (2013)

However, it is in contrast to previous studies that found a positive connection between board independence and Tobin-Q whether in developed countries like Cordeiro *et al.* (2007), Florackis (2005), Khanchel (2007), Mura (2007), Shan and McIver (2011) and Yawson (2006) or in developing countries such as Black *et al.* (2003), Choi *et al.* (2007), Hsu *et al.* (2009), Jackling and Juhl (2009), Kang and Kim (2011), Nuryanah and Islam (2011) and Saibaba and Ansari (2011).

Also, this finding is not in line with the finding of some studies that found no association between board independence and Tobin-Q in the developed countries (Belkhir, 2005; Hu *et al.*, 2010; Siala *et al.*, 2009; Yue *et al.*, 2008) and in developing countries (Al-Matari *et al.*, 2012b; Garg, 2007; Ibrahim & Abdul Samad, 2011; Kyereboah-Coleman, 2007; Ghazali, 2010).

One reasonable explanation for the insignificant association between board independence and Tobin-Q is the power of the CEO power within the council. In addition, because the

board is non-executive, it lacks the abilities to participate in the design and development of the company's strategic plans.

The second reasonable explanation for the insignificant association between board independence and Tobin-Q is that although the majority of the board is non-executive, a strong recruiting policy that contributes to the selection of highly qualified persons may be lacking. These persons may be able to add new plans that would help companies to make right decisions. Therefore, this policy assists in improving the performance of companies.

A third reasonable explanation for this finding is the lack of provision of non-executives of new and contemporary idea that leads to develop and improve the company's performance. This includes providing clear visions, plans and strategies to keep pace with the changes occurring in the local and international markets. This, in turn, leads to attract investors and contribute to the company value. In other words, non-executives do not contribute to the company's strategy and company performance.

7.3.2.1.3 Board Meeting and Tobin-Q

In line with the resource dependence theory, the result of this study found a positive significant association between the board meeting and Tobin-Q as shown in Table 7.1. This finding suggests that the board meeting is associated with higher firm performance. This finding is also supported by the Code of Corporate Governance in Oman which mandates that the board shall have a meeting at least 4 times a year with a maximum of 4

month gap between two meetings in order to revise and solve any problems faced by the board through the year.

This finding is similar to some prior studies that confirmed a positive significant relationship between board meeting and Tobin-Q whether in developed countries (Khanchel, 2007) or in developing countries (Kang & Kim, 2011; Sahu & Manna; 2013). On the other hand, this result is different from those prior studies who found a negative association between board meeting and Tobin-Q like Kamardin (2009), or no significant association such as Kyereboah-Coleman (2007).

As the theory of resource dependence postulates that the board meetings help the board to evaluate and pursue a board business in a timely manner and to solve any problem immediately (Pearce & Zahra, 1992; Pfeffer, 1987). Hence, the effectiveness of board meetings can be reflected in enhanced firm performance.

It was also argued by Vafeas' (2000) that the frequency of the board meeting is a crucial activity that can assist in enhancing firm's operating performance. Therefore, the board should be ready to increase the frequency of their meetings when the circumstances call for strict supervision and control (Khanchel, 2007; Shivdasani & Zenner, 2002).

7.3.2.1.4 Board Change and Tobin-Q

This study predicts that the board change influence the aspects of the firm, including strategy, policy and decision making. This study hypothesised a relationship between the

board change and Tobin-Q. The finding is similar to the accounting measurement and it is in conflict with the expectation as apparent in Table 7.1. This relationship was found to have not been associated with Tobin-Q which does not support the hypothesis.

The insignificant association between board change and Tobin-Q may be justified by the ambiguous insight of the variable in the Omani Code of Corporate Governance. It is hence important that regulators stress on this change every year. Another reason may be the ineffective company policy of appointing persons to the firm which should be those with the right education, experience and knowledge. Government representative in securities commission should modify its code and apposite one article to stress on the importance of the change of mandate. Government representative in securities commission should also encourage all listed companies to employ obligations when changing member of the board.

7.3.2.1.5 The Role of Secretary on the Board and Tobin-Q

As explained earlier, the role of secretary on the board is crucial where the secretary's primary role is to ensure that firm's business is in the right direction. Because of that, this study expected a relationship between the role of secretary on the board and Tobin-Q. However, the finding as reported in Table 7.1 found no significant association between the role of secretary on the board and Tobin-Q.

The justification behind the insignificant relationship between the secretary of the board's role and Tobin-Q, is the lack of attention given to the role of secretary of the board to all

listed companies which would in turn produce poor outcome. Hence, regulators should encourage all listed companies to maintain the role of secretary of the board and to acknowledge its significance.

Moreover, the weak contribution of the secretary of the board in firm performance can also be attributed to the ineffective role play by the secretary in monitoring the tasks and coordinating the operation.

In general, the secretary of the board has an important role in both private and public companies and should be stressed for all sectors to effectively communicate and achieve the firm's target and maximise shareholder's wealth. This issue is compounded by the fact that there has been no strict ruling of compliance that has been established by regulators in security commission. This calls for a government representative in security commission to enforce a ruling that mandates all listed companies to follow the ruling of the secretary's role according to the recent changes of international codes. Furthermore, companies and security commission should corroborate that all listed companies are able to enhance their policies to improve their performance.

7.3.2.1.6 Legal Counsel and Tobin-Q

This study found a significant negative relationship between legal counsel and Tobin-Q as illustrated in Table 7.1 which does not support the hypothesis H6b.

The insignificant relationship between the role of legal counsel and Tobin-Q may be attributed to the lack of understating of its importance which will minimise court allegations and provide insurance between future contracts with other companies. This legal counsel works to minimise misunderstanding between a company and others parties. In addition, the insignificant relationship may be explained by the fact that the legal counsels in many Omani companies lack experience and knowledge concerning the business environment and the current situation in Oman.

7.3.2.1.6 Foreign Member on the Board and Tobin-Q

This study expected that the number of the foreign members affects the firm performance as measured by Tobin-Q. However, the result found insignificant effect of foreign members on the board on Tobin-Q

The reason behind the insignificant relationship between foreign members on the board and Tobin-Q is that the foreign members may not be as knowledgeable and authorised to make decisions with limited information at their disposal. Another possible explanation for this insignificant effect may be that the company does not disclose full information of the firm to foreign member. As such, the Omani Security Commission should determine the selection conditions of foreign members and their involvement in work, their rights and duties, for the betterment of the firm's performance. For instance, currently foreign members are not provided with materials and moral incentives that could assist them to work seriously in order to achieve the goals of the company.

7.3.2.2 Audit Committee Characteristics

7.3.2.2.1 Audit Committee Size and Tobin-Q

In contrast to the hypothesis, the result of this study found an insignificant association between audit committee size and Tobin-Q as reported in Table 7.1. This result is not in line with the Blue Ribbon Committee which states that in order to improve the effectiveness of a corporate audit committee (BRC, 1999), the audit committees should be established. It is also recommended that audit committees should have a minimum size of three members and should consist of solely NEDs. Along the same line, in the Omani Code of Corporate Governance, the audit committee plays the main role to oversee the internal control framework effectiveness and its review of the financial reporting process in order to enhance the performance of firms.

The result of this study was similar to those of previous scholars like Kyereboah-Coleman (2007) and Nuryanah and Islam (2011) who found no relationship between audit committee size and Tobin-Q. On the other hand, this result is in contrast with some prior studies that found a positive and significant link between audit committee size and Tobin-Q whether in developed countries such as Khanchel (2007) and Reddy *et al.* (2010) or in developing countries like Black *et al.* (2003) and Heenetigala and Armstrong (2011).

A probable reason for insignificant finding of audit committee size and Tobin-Q is that in the context of Oman, an audit committee is not as important as it is in developed

countries. This result matches the significant results of an audit committee size, which indicates that the role of specific elements of board practices in developed countries upon firm performance is non-existent in Oman. Similar to the insignificant result of board size, this result indicates that in developing nations like Oman that is characterised by underdeveloped capital markets and weak external CG mechanisms, the market participants deem independent boards to be more important compared to the board size of the audit committee strength. Because external governance mechanisms are not as effective, board independence, reflected by independent commissioners' composition and leadership structure, is preferred by the capital market in Oman.

However, other studies concentrated on the AC effectiveness as opposed to their sizes as they do not deem AC size to be an important factor in improving the committee's effectiveness. For the effectiveness of AC, it should be made up of independent, expert and well-informed members and should wield sufficient authority (Mohiuddin & Karbhari, 2010).

7.3.2.2.2 Audit Committee Independence and Tobin-Q

On the basis of the agency theory and the resource dependence theory, this study hypothesised a positive relationship between audit committee independence and Tobin-Q. However, the finding reveals an insignificant link between audit committee independence and Tobin-Q which does not support the hypothesis H9b.

However, this result agrees with those of previous studies, like Al-Matari *et al.* (2012a+b), Kota and Tomar (2010) and Kyereboah-Coleman (2007) that found an insignificant association between audit committee independence and Tobin-Q.

But, the result of this study is not similar to those previous studies that revealed a positive relationship between them whether in developed countries such as Dey (2008) and Khanchel (2007) or in developing countries like Abdullah *et al.* (2008), Nuryanah and Islam (2011) and Saibaba and Ansari (2011).

One explanation for the insignificant relationship between audit committee independence and Tobin-Q is that it may be insufficient for an audit committee to achieve its monitoring responsibilities to enhance firm's value. There should also be a large majority of expert-independent audit committee members serving on the audit committee to improve the value of the firm (Al-Matari *et al.*, 2013a).

A second possible reason behind this finding is that it may be significant to appoint individuals with technical expertise and experience in order to guarantee value creation. Therefore, the Omani capital market authority must be a leading example for all listed companies to appoint persons with higher qualifications in order to improve long-term company plans.

A third plausible justification for the obtained result is that may be the board independent members do not have a friendly relationship with all members of the board and hence cannot not work with them as a team, make the right decision and achieve firm targets.

7.3.2.2.3 Audit Committee Meeting and Tobin-Q

This study hypothesised that there is a relationship between audit committee meeting and Tobin-Q. The result of the study showed that there is a negative significant association between audit committee meeting and Tobin's Q. This means that, an audit committee meeting does not contribute in enhancing performance. This result is not in line with the Code of Corporate Governance in Oman, regarding mandating the committees to hold meetings at least four times a year with a majority of independent directors.

When comparing this result with the existing literature, it can be said that this result is similar to some previous studies such as Hsu and Petchsakulwong (2010) that found that there is a negative significant relationship between audit committee meeting and Tobin-Q in Saudi Arabia. Also, this finding is not in line with previous studies that found a positive relationship between audit committee meeting and Tobin-Q like Khanchel (2007) in the US and Kang and Kim (2011) and Kyereboah-Coleman (2007) in Korea and Africa respectively.

A possible reason for negative significant finding of audit committee meeting and Tobin-Q is that as stated by Rebeiz and Salame (2006), the meeting quality matters most and that the frequency does not always improve the firm performance. Therefore, the frequency of audit committee meetings may notably increase during financial distress or during controversial decisions involving illegal or erroneous activities.

Another possible explanation for the negative significant finding is that; the frequency of audit committee meetings are not always useful, because the time that NEDs spend together is limited and spent for activities other than exchanging meaningful ideas among themselves and with management. This notion has been acknowledged as a natural result of the fact that the agency of such meetings is set by the CEO.

7.2.2.3 Executive Committee Existence and Tobin-Q

Although executive committee is important to improve company's performance, there has been a lack of empirical studies that have investigated its effect on firm performance. This study examined the relationship between the executive committee and firm performance to contribute to the very few researches in this regard.

On the basis of the agency theory and the resource dependence theory, this study hypothesised that there is a relationship between the executive committee and Tobin-Q. The finding reveals a negative significant link between the executive committee and Tobin-Q. Therefore, hypothesis 11b is supported. This study suggests that the executive committee is associated with lower firm performance.

One plausible explanation for the negative significant association between the executive committee and Tobin-Q is the fact that executive committees in Oman are not considered as important as compared to other committees. This result indicates that the role of some specific board practices in Oman does not exist. More importantly, the Code of Corporate

Governance in Oman largely ignores the importance of the executive committee and its value towards enhancing the firm performance.

Moreover, this insignificant relationship between executive committee size and the firm performance may be attributed to the weak external corporate governance mechanisms in Oman, which is associated with a developing capital market. Because of the ineffectiveness of external governance mechanisms by independent commissioner composition, a leadership structure is opted in the Omani capital market.

7.4 Implications of the Study

This study has enlarged the literature of prior studies that examined the relationship between CG mechanisms, namely board of directors' characteristics (board size, board independence, board meeting, board change, secretary role, legal counsel and foreign member on the board), audit committee characteristics (size, independence and meeting), executive committee and firm performance (ROA and Tobin-Q) of the public listed companies in Omani MSM.

The majority of the studies regarding the CG and performance relationship have been conducted in the developed countries as extensively explained throughout this study. However, there has been a lack of studies conducted in developing countries in general and the Gulf countries in particular. So far, there are few studies that examined the relationship between CG and firm performance, such as Al-Hussain and Johnson (2009) in Saudi Arabia, Aljifri and Moustafa (2007) in the UAE, Al-Matari *et al.* (2012, 2012b)

in Saudi Arabia, Al-Matari *et al.* (2012) in Kuwait, Al-Najjar (2013) in five middle east countries, Ghabayen (2012) in Saudi Arabia and Najjar (2012) in Bahrain and unique studies in Oman in particular that elaborated on the CG and its impact on corporate performance in Oman (e.g. Al-Matari *et al.*, 2012 and Al-Matari *et al.*, 2012a, 2012b). In other words, there is a paucity of literature that examined this association in the Gulf countries.

This study has attempted to study the said relationship in Oman. Hopefully, this study will benefit the owners of companies in Oman, and all users in general as it highlights the relationship between corporate governance mechanisms and firm performance in Omani companies. As a matter of fact, the application of the principles of good governance will help in attracting investors (whether local or foreign) to the country and give them the confidence to invest in a country characterised by good environment, as this investment will generate profits in both short term and long term.

By and large, the previous studies examined the relationship between the board of directors and firm performance. Almost all of them focused on the board size, board independence, the board meetings and others, but they neglected to investigate the relationship between board change, secretary role, legal counsel and foreign member on the board and firm performance. With due respect to the importance of these variables' integration with the board of directors in order to improve firm performance, the present study took them into account.

Moreover, although this study was consistent to prior researches, which studied the integration between board characteristics and audit committee characteristics to firm performance. It has added board committee in this integration, because it has an important role in encouraging all listed companies to improve their performance in order to establish a strong infrastructure of investments.

Due to the inconsistencies regarding the relationships between the board of directors' characteristics and firm performance, this study attempted to re-examine this relationship in the context of Oman as an example of developing countries.

From the theoretical perspective, although there were many theories that had relative relationship to CG such as agency theory, resource dependence theory, stewardship theory, institutional theory, stakeholder theory, transaction cost theory, political theory, ethical theories, tournament theory and others, this study chose popular ones including agency theory and resource dependency theory, which have become prominent over recent times. In consistence with the recommendation of Al-Matari *et al.* (2012a) to test some other theories against firm performance, namely stakeholder theory, stewardship, resource dependence theory and others, this present study also considered the agency theory and resource dependence theory as the theoretical foundation of the study.

As for the agency theory; a theory generated from the study by Berle and Means (1932) with regards to the separation between ownership and control in large firms, the most common studies dedicated to it came from Jensen and Meckling (1976). The theory has

its basis on the relationship between the principal (the owner) and the agent (the manager). In current firms, the separation between ownership and management provides the context for the function of agency theory. The most significant premise behind the theory is that management is often driven by their personal interests rather than the shareholders' interests and to increase shareholder value. For example, management may be more inclined to have luxurious offices, company cars and items that satisfy their cravings, while owners pay for the price.

This theory may be the basis of firm governance through different internal and external mechanisms (Roberts *et al.*, 2005; Weir *et al.*, 2002) as these mechanisms are created to guarantee that the interest of agents and principals are aligned to protect shareholders' interests and to lessen agency costs (Davis, Schoorman & Donaldson, 1997).

This statement is shared by Demsetz and Lehn (1985) who claimed that the primary aim behind CG is to tackle agency problems through the oversight of management behaviour and examination of the financial reporting process as opposed to directly improving corporate performance. This enables CG mechanisms to lessen agency costs and safeguard the interests of shareholders by monitoring management activities and aligning management and shareholders' interests.

Consistent with the previous recommendations related to agency theory, the number of board members should not be so many to make timely and quality decision, but they should be enough to monitor firm operations with freedom. The board meeting should be

conducted at the appropriate time. The audit committee is very valuable in monitoring and evaluating company transactions in a timely manner and in solving any problem faced during work. The board is very important to improve performance of the company and thus, it should consist of knowledgeable individuals that will improve and enhance trust in the company in both short and long term. Therefore, the board has the freedom to appoint or select any person or committee who has the ability to improve the performance of the company, because the main objectives of any company are to achieve company's aims successfully and to make profits.

Furthermore, from the perspective of resource dependence theory, the theory states that boards are chosen to increase the supply of required firm resources (Hillman & Dalziel, 2003; Klein, 1998; Pfeffer & Salancik, 1979; Pfeffer, 1972). According to this theory, the board of directors comprises of individuals who span the boundary and obtain resources from the surroundings (Pfeffer, 1973). The resource dependence theory further postulates that directors are valuable resources that achieve business operations while fulfilling their monitoring roles (Hillman *et al.*, 2000).

The resource dependence theory also states that the business environment is full of external factors that may cause uncertainty and external dependencies (Daily, Johnson & Dalton, 1999). Correspondingly, firms have to handle the factors that produce uncertainties so that they may thrive in dynamic and competitive surrounding. Directors are considered as the linkage between firm and these factors as they help firms make effective decisions.

This theory provides a theoretical base for the role of the board of directors in the firm (Johnson *et al.*, 1996; Hillman *et al.*, 2000), while an external board of directors' appointment helps in accessing resources that are crucial to the firm's success (Johnson *et al.*, 1996). To reiterate the role of resource dependence, external directors offer resources to the firm such as information, skills and network to important constituents like suppliers, buyers, social groups, public policy decision makers, and legitimacy (Hillman *et al.*, 2000).

The board of directors is one important monitor that encourages top level executives to consider the distinction between decision control and decision management (Fama & Jensen, 1983). The board's primary responsibility is to determine the compensation of CEO in terms of structure and value. In an ideal situation, the structure of compensation would work to match the interests of CEO with that of shareholders' according to the evaluation of firm performance and the contribution of CEO to management. In situations where the board is dependent on CEO's control, it is challenging to evaluate CEO's performance and to offer a compensation package that ties rewards to shareholders (Fama, 1980). Intrinsically, the board should comprise of independent directors with the incentives to offer high quality oversight (Abdullah *et al.*, 2008; Finkelstein & D'Aveni, 1994).

As extensively explained in the literature review and methodology chapters, any theory alone may not be enough to cover the relationship between CG and firm performance. Thus, two theories are employed to explain the situation of this study with regards to;

rules, regulations, culture, environment, the economy and systems, the Omani companies follow in order to achieve their objectives as planned. The integration between the two theories (agency theory and resource dependence theory) provides a clear understanding of the relationship between CG mechanisms and firm performance.

Moreover, the findings of this study are not similar to previous studies in the developed countries because the guidelines and structure of CG are different. The differences in results may be attributed to the process and procedures of the code of corporate governance in Oman that have not been updated since their establishment in 2002. Although the Omani Security Commission in Oman may not be at par with the development in the global economy, yet some committees are established in almost all public companies listed on the MSM that are not related to the Code of Corporate Governance in Oman. Hence, the capital market authority must update this code in order to keep pace with developments in the world to improve and to win the trust of both local and foreign investors, which in turn would lead to maximised wealth of shareholders.

Furthermore, the differences in results may be linked to the differences underlying in Omani culture, environment, economy, structure of CG, regulations, laws and others, so that the government must study all codes in the world and establish a good and flexible code consistent to global codes in order to encourage investors to invest without risk concerns.

According to the board of director's characteristics (board size, board independence, board meeting, board change, legal counsel, foreign member on the board), audit committee characteristics (size, independence and meeting), executive committee existence with ROA is similar. Based on this association, the finding indicates that the agency theory and resource dependence theory are not applicable in Oman. However, the result showed that the secretary role on the board is applicable to agency theory in Oman.

From another firm's proxy, namely Tobin-Q, board of director's characteristics (board independence, board change, legal counsel, foreign member on the board), audit committee characteristics (size and independence) the association with Tobin-Q is similar. Based on this association, the finding indicated that agency theory and resource dependence theory are not applicable in Oman. However, the results of board size, board meeting and legal counsel to Tobin-Q, the resource dependence theory is found to be more applicable than agency theory. On the contrary, audit committee meeting and executive committee existence, agency theory is found to be more applicable than resource dependence theory. Ultimately, the practice of corporate governance in Oman is consistent with that of resource dependence theory as compared to agency theory because the practice of CG is still in its infancy stage and it needs to be modified and updated until it is at par with that of developed countries.

7.4.2 Implications to Practice

The present study is of great value to companies, regulators, policy makers and shareholders in Oman in various ways. First, this study's results offer valuable insight into potential investors, stakeholders and the general public. This allows a better understanding of non-financial companies' characteristics, the role of CG mechanisms of firms on the firm performance.

Second, the present study also offers some practical implications for management. It is important that management becomes aware of the fashion in which board governance characteristics and various types of board diversity will impact the value of the firm. Their awareness of these characteristics would enable them to select suitable methods for handling the board of directors, while keeping in mind that the benefits of increasing firm value through improved board governance are not identical throughout all firms.

Moreover, the present study's findings invariably present various viewpoints that could help government, scholars, shareholders, institutional investigations and other relevant stakeholders. According to the result of this study, information obtained from non-financial CG is more significant than the overall classification of governance when it comes to evaluating company's performance. The careful selection of companies that improves their CG may assist investors in having superior chances of obtaining higher returns.

Based on the results, good business governance is linked with lower cost of equity and assessment. Large investors may be capable of reaching superior assessment of their activities, which eliminates governance shortcomings. In addition, the result shows that companies enhance their corporate governance performance over time, and the governance change is more significant than the level of government in identifying the company's performance. This finding is useful for listed companies to improve their corporate governance in order to enhance their operational performance, minimise issues of free cash flow and low cost of capital, which in turn would increase firm performance.

Third, the positive significant relationship between board size and Tobin-Q has a practical implication to corporate governance in Oman. This finding supports resource dependence theory which suggests that performance could be better when the board has many members because of the diverse experience and qualifications of the members in maximising shareholders' wealth.

Fourth, the negative insignificant relationship between board independence and both measurements of firm performance (ROA and Tobin-Q) indicate the practical implication of CG in Oman. The members may not be selected according to their experience, qualification and other characteristics that assist in maintaining the role of the board's independence. This result is not consistent with global code and Omani Code of Corporate Governances that recommend majority of the board to be independent. As such, regulators and companies ought to emphasise the importance of having non-executive directors on the board.

Fifth, the positive significant relationship between board meetings and Tobin-Q has some practical implications of CG in Oman. This may be among the important areas that CMA should emphasise on to the board in Oman in order to provide supervision and solutions to problems.

Sixth, the negative significant association between secretary role and ROA also has an implication to corporate governance in Oman. This indicates that the CMA should encourage companies to appoint a secretary to organise all contracts of company with others and take consultation from the office. In other words, this role helps to reduce conflict between board and others.

Seventh, the negative relationship between audit committee meeting and Tobin-Q has an implication to CG in Oman. This indicates that CMA should the positive significant connection between executive committee independence and Tobin-Q has practical implication to Omani CG. It is, therefore, important for regulators and companies to emphasise the importance of having non-executive directors on the committee. More specifically, this result is consistent with global codes of corporate governance and Omani Code of Corporate Governance which state that executive committee independence helps in overseeing company transaction.

Eighth, the negative relationship between executive committee existence and Tobin-Q has an implication to CG in Oman. This indicates that the CMA should bring up the importance of the presence of non-executive directors in the committee to regulators and

companies. More specifically, this result is consistent with global codes of corporate governance and Omani Code of Corporate Governance that suggest the audit committee independence helps monitoring company transaction all the time without complying to the board authority.

Ninth, the results of board size, board independence, board meeting, board change, legal counsel, foreign member, audit committee size, audit committee independence, audit committee meeting and executive committee's existence showed no significant relationship to ROA. This is similar to board independence, board change, secretary role, legal counsel, foreign member, audit committee size, audit committee independence were all revealed not to be related to firm performance (ROA and Tobin-Q).

To conclude, the contrasting results between the present study and prior studies in other countries contribute to the debate dedicated to CG. This reinforces the claim by Haniffa and Hudaib (2006) that governance structures created to improve corporate governance should not be blindly employed. However, the business environment and the economic characteristics of the country, including stock market regulations, requirements of disclosure, structures of firm ownership and culture should be taken into consideration.

7.4.3 Implications to Policy Makers

The present study went through variables addressed in prior studies which reported contrasting results of the relationship between independent variables; namely board of directors' characteristics (board size, board independence, board meeting, board change,

secretary role, legal counsel and foreign member on the board), audit committee characteristics (size, independence and meeting), executive committee and four control variables, firm size and leverage, industry and time period with firm performance (ROA and Tobin-Q). Although the efficiency of CG characteristics influences the environment in which the firm is operating in, prior studies failed to present evidence of stakeholders in other environments that were not investigated. This study is an extension of prior studies as it provides evidence to Omani regulators, owners, management and government with regards to the relationship between these variables and firm performance. It is important to reiterate that CG practices differ from one country to another according to culture and other factors. The Omani regulators should also realise the importance of some elements in the CG structure to be mandated by all the listed companies, so that the investors can have the necessary information to take investment decisions.

7.5 Limitations of the Study and Suggestions for Future Research

This study, like previous studies, has limitations which are discussed in this section. First, the research design employed in the study is limited to listed companies in the MSM with emphasis on non-financial firms and exclusion of financial and non-listed companies. Hence, the outcome's validation may not be appropriate for financial and non-listed companies. Making a generalisation which is applicable to all sectors should therefore be made with caution. This study considered five years; 2008, 2009, 2010, 2011 and 2012

and this short period of the study may not reflect all operations of the sample companies. So, future researchers should consider the extension of this period and to all sectors.

Second, this study examined the joint effect of integration between the board of director characteristics, namely board of directors' characteristics (board size, board independence, board meeting, board change, secretary role, legal counsel and foreign member on the board), audit committee characteristics (size, independence and meeting), executive committee on the firm performance. This study's limitation also derives from the nature of data gathering; in Oman, annual reports of listed companies are limited compared to their counterparts in other countries. This study recommends that future researcher should examine the effect of some other variables such as ownership structure, purchase committee, remuneration committee and other committees' relevance to evaluate performance of the company.

Third, this study examined the effect of some variables related to board of directors' characteristics, namely size, independence, meeting, board change, the role of secretary on the board, legal counsel and foreign member on the board on the firm performance. However, future studies must consider taking into account some other variables like CEO tenure, CEO compensation, meeting attendance, remuneration, attending annual general meeting, board members remuneration, the participation of members of the board of directors on the boards of other companies and other variables' significant role in improving firm performance.

Fourth, although this study examined the effect of the audit committee and the executive committee on firm performance, it suggests future researchers to investigate the integration of internal audit characteristics with other committees on the board in order to enhance the performance of the company.

Fifth, this study examined the direct relationship between CG and firm performance. This study recommends future researchers to examine board diversity such as gender, age, foreign members on the board and experience, qualification and others that have valuable effect as moderator variables. This study also suggests applying this moderator's variable for other committees like audit committee and executive committees, etc. Moreover, this study recommends future study to consider studying the mediating effect of the audit quality on the relationship between audit committee and firm performance. This study considered two proxies of performance namely ROA and Tobin-Q and thus future researchers may consider investigating the relationship between corporate governance with other proxies like Return on Equity, Return on Sales, Return on Investment, Profit Margin, Operating Cash Flow, Operation Profit, Growth in Sales, Return on Capital Employed, Expense to Assets, Cash to Assets, Sales to Assets, Expenses to Sale, Labour Productivity, Cost of Capital, Market-to-Book Value, Abnormal Returns; Annual stock return, Dividend Yield, Price-Earnings Ratio, Log of Market Capitalization, and Stock Repurchases, in order to enhance performance both in the long and short term.

Seventh, one of the main objectives of this study was to provide a clear picture about regulations and structure of CG in Oman. However, future studies could focus on

emerging markets in the gulf countries and conduct a comparison among all gulf countries. More attention, as explained in previous chapters, is needed due to the lack of studies in developing countries in general and in the Gulf countries in particular. Therefore, future researchers should intensify their efforts in many studies in the Gulf States as it is of utmost importance.

Eighth, this study only examined the agency theory and resource dependence theory. On the other hand, future studies could extensively examine the tournament theory with firm performance because there is a lack of studies in this field. Future studies could also examine the relationship between CG and firm performance in light of other theories such as stewardship theory, institutional theory, stakeholder theory, transaction cost theory, political theory, ethical theories, tournament theory, etc.

7.6 Conclusion of the Study

Essentially, this study examined the relationship between CG mechanisms, namely board of directors' characteristics (board size, board independence, board meeting, board change, secretary role, legal counsel and foreign member on the board), audit committee characteristics (size, independence and meeting), executive committee and firm performance (ROA and Tobin-Q) of the public listed companies in Omani Muscat Securities Market (MSM). This study comprised of non-financial sectors at the end of 2008, 2009, 2010, 2011 and 2012.

More specifically, as mentioned earlier, the study's motivation lies in the gap in extant literature and few evidences in the context of developing countries, particularly in Oman. This study enhances the understanding of CG mechanisms influencing firm performance, especially with the unique culture and business environment of Oman. Although Oman has a unique investment environment to encourage both local and foreign investors to invest without risk consideration, yet the results did not totally support the hypotheses. This may be attributed to the lack of good practical implications in some companies. Therefore, government representatives in stock market authority should make it mandatory for all companies to apply the code of corporate governance. The Stock Market Authority also must update the code till it becomes consistent with global code of corporate governance in order to develop performance.

The resource dependence theory is more applicable to most Omani businesses, as the board diversity facilitates the enhancement of performance through diversity of members such as experience, qualification, foreign member and others. This study proved that the agency theory is not applicable in the Omani environment. Although CG is practiced by Omani companies, further improvements are still needed to strengthen them.

Perhaps, the Code of Corporate Governance should be made flexible to accommodate the type of businesses. Some requirements like the duties of the board independence, the board diversity, namely experience, qualifications, foreign member, the board commitment, among others, may discourage businesses from floating their shares in the capital market.

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