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EFFECT OF CORPORATE GOVERNANCE ON ORGANIZATIONAL PERFORMANCE: AN EMPIRICAL STUDY OF NEPALESE COMMERCIAL BANKS.

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Abstract:
There is no any doubt that corporate governance intended to well and effective functioning of enterprises incorporating the interest of all the stakeholders equally leading to better organizational performance. The major objective of this research is to explore the effect of corporate governance in the organizational performance of Nepalese commercial banks. To address the study objective, it has used descriptive and analytical research design. The study has taken 175 banking staffs of five commercial banks of Nepal as the respondents. The construct reliability of this study is greater than the cut-off level 0.7 of Nunally (1978). This study found that Nepalese banking staffs are more committed towards their work and satisfied with the practice of corporate governance in their respective banks. It shows that all study variables are positively related with each other. Among independent variables; transparency & disclosure and auditing & compliance of law have stronger positive relation with dependent variables; financial and non-financial performance of organization. This study concludes that there is significant impact of corporate governance on organizational performance in Nepalese banking industries and it plays an important role in improving the overall organizational performance.

Key Words: Corporate Governance, Performance, Commercial Banks, Nepal.

1. Introduction

Corporate governance supports an organization during the process of building integrity, ensuring transparency and accountability. It also ensures that effective channel of information disclosure is maintained to foster good corporate culture (Gyawali, 2018; Owiredu and Kwakye, 2020). Corporate governance is the critical aspect in every corporation which encourages decent corporate activities following the ethical behaviors (Kirado, 2019). Corporate governance ensures an implementation of a set of rules which facilitates the organizational activities to be managed and establishing a system by which corporate activities can be directed and controlled (Cadbury, 1992; World Bank, 1999). Corporate governance incorporates, corporate structures, culture, policies and strategies and the ways of dealing various stakeholders (Barrett, 2002; Delima and Ragel, 2017). Corporate governance concern to the legal way and manner by which resources available to an organization are sensibly used to achieve the overall corporate objective of an organization (Tukur & Bilkisu, 2014; Obamiro, Tijani and Ojo, 2019).

Good corporate governance requires sound internal and external governance which respond effectively and adequately to the internal as well as external stakeholders to get competitive corporate advantages of market (Tura, 2012; Kyere and Ausloos, 2020). The benefits of good corporate governance are ensuring whether the environment of the business is transparent and fair or not and whether the companies are accountable towards their operations or not. Inversely, poor corporate governance helps wastage, disturbance in management and promote unethical behaviors (Chen and Lee, 2012). The importance of corporate governance in modern organization increasing day by day. Nevertheless, the different nature, types and size of organization, only strong corporate governance brings better performance of business in long terms (Al-Azzam, Al-Qura'an and Al-Mohameed, 2015). Corporate governance purposes to support effective monitoring and well-organized functioning of business through fairness and transparency in operations and enhancing disclosures for protecting interest of different stakeholders. The structures of corporate governance are expected to help the better performance of organization through quality decision making (Arora and Bodhanwala, 2018; Goel, 2018).

Organizational performance is the result of optimum utilization of organizational resources and means which ensures the accomplishment of the corporate objectives (Jenatabadi, 2015). The performance is the summation of all methods, procedures and measures that will lead executives of organization for appropriate decision making which leads efficiency and effectiveness of the organization (Neely et al., 2004; Felizardo, Felix and Thomaz, 2017). Performance is qualitative and quantitative indicator used to show weather the organizational financial and non-financial objectives are met or not (Sinclair and Zairi, 1996; Neely, 2004; Tangen, 2005; Richard et al., 2009; Popova and Sharpanskykh, 2010; Felix and Thomaz, 2017). Organizational performance is the basis of corporate success providing guidance and feedback for preparing corporate strategies and effective implementation for achieving corporate objectives (Randeree and Al Youha, 2009; Almatrooshi, Singh and Farouk, 2016).

Good corporate governance has a link with performance for the sustainable organizational success. It plays an important role for improvement of profitability which is essential to attain corporate objectives (Gill and Mathur, 2011; Kirado, 2019). Corporate Governance ensures transparency, accountability and professionalism in the financial system that enhances the credibility and acceptability to the shareholders, employees, present and potential investors, customers, lenders, governments and general public. (Attiya and Iqbal, 2010). Corporate governance is more important for financial institution as there is an ever-present risk of moral hazard. The establishment of the corporate governance codes used to eliminate any scope of discrepancies from regulatory standards by financial intuitions, either voluntarily or involuntarily (Anwar, 2009; Rashid et a., 2020).

In developing countries like Nepal, financial sector plays an important role in overall growth of economy. Bank and financial institutions are the key institutions of the financial sectors, whose performance and growth are key for the growth of national economy. The empirical studies shown that the importance of strong corporate governance in the management of organization in spite of different nature and size of organizations in both developed and developing countries. Hence, this study is aiming to see the role of corporate governance in the organizational performance of Nepalese commercial banks.

2. Literature Review

Corporate governance is accomplished through established structures and practices where structures recognize distribution of rights and responsibilities among various corporate stakeholders and governance practices comprise board operations such as; appointment, functioning, compensation and conflicts management (Aguilera and Jackson, 2003; Dewji and Miller, 2013; Grace, Vincent and Evans, 2018). Corporate governance propagates a system in an organization which facilitate in managing the organization, setting the goals and objectives, monitoring and assessing the risk for improving the organizational performance Hamilton, 2003). The major objective of corporate governance is to ensuring the appropriate, comprehensive and correct financial information of organization which can fulfill the interest of all the stakeholders (Burak, Erdil and Altindag, 2017) Several studies have been conducted on corporate governance and performance of organization. Many researchers agree that good corporate governance leads to high organizational performance (OECD, 2004; Amaoko & Goh, 2015). Brown and Caylor (2004) in their study established a positive relationship between corporate governance and firm performance. Grove et al. (2011) states that there is a strong association between corporate governance and financial performance of an organization. Grace, Vincent and Evans (2018) indicated that corporate governance has a statistically significant influence on the performance of financial institutions.

The research outcomes of Rashid et al. (2020) show that the productivity of the Bangladeshi banks is significantly influenced by corporate governance. Gadi, Emesuanwu and Shammah, (2015) in their study examine corporate governance and financial performance of Micro Finance Banks in North Central Nigeria and found that composition of board committees has significant relationship with banks financial performance. Ogbechie & Koufopoulos (2010) investigated the relation between corporate governance and board practices in the Nigerian banking industry and discovered that a standard board size comprising of all board committees is ideal for any organizational set up. Similarly, Adebayo, Ibrahim, Yusuf & Omah (2014) studied corporate governance and performance of organization and found that board size, board skills, management skills and size of audit committee are positively associated with performance in organizations. Ammar, Asif & Ammar (2013) examined Corporate governance and performance in the Pakistan context and revealed a positive association between board size and firm performance. Kyere and Ausloos (2020) in their empirical study of 252 non-financial firms of United Kingdom indicates a positive or a negative relationship, but also sometimes no effect, of corporate governance mechanisms on their financial performance.

Corporate governance seeks for an accountability among shareholders, the boards of directors and the management of corporate entity. The strategic decision-making process is the key to achieve corporate objective of an organization. Furthermore, the prerequisites of good corporate governance like impartiality, transparency, accountability and responsibility could provide maximum protection from financial crisis and can strengthen the access to capital (Randeree and Al Youha, 2009). Hence, good corporate governance assures adequate valuation, higher profit, higher sales growth and lower capital expenditure (Drobetz et al., 2003 as cited by Oino and Itan, 2018). Cadbury report (1992) stressed that good application of corporate governance could facilitate an organization with the output like shareholders wealth maximization and efficient utilization of firms' assets. Good corporate governance follows the principles like transparency, accountability, responsibility, independence and fairness which are directly proportionate with the corporate performance. Good corporate governance parallelly uplifts the organization's profitability and firm performance which results into the successful operation of an organization (Nur'ainy et al., 2013). OECD (2004) stresses that best corporate governance practices must incorporate formal governance policies, codes and guidelines, role of board of directors and association with management, strong shareholder rights, internal control system, transparency, disclosure and sustainability.

3. Research Methodology

This paper is concentrated on the examining the contribution of corporate governance in the organizational performance of Nepalese banking institutions. The study used descriptive and analytical research design to address the study objective. Five Nepalese commercial bank out of total 27 commercial bank operated in Nepal are taken as sample for this study. Both primary and secondary sources of data have been employed for the result. Primary data are collected through a set of questionnaires which are design on five-point Likert scale and secondary data are collected through different published and unpublished reports of banks. Responses from 175 employees from different branches of sample five commercial banks are used for data analysis. The collected data are processed and analyzed using SPSS (version 23), MS-Excel, descriptive statistics, correlation analysis, regression analysis. In this study, several factors of corporate governance (transparency & disclosure, board size, auditing & compliance of law and board composition & independency) are considered as independent variables and organizational performance is considered as dependent variable; which is represented by financial and non-financial performance of organization (profitability, liquidity, job satisfaction and employee's commitment). The variables in this study are selected with help of the studies of Delima and Ragel (2017); Burak, Erdil and Altindag (2017); Oino and Itan (2018); Kiradoo (2019); Owiredu and Kwakye (2020); Kyere and Ausloos (2020). The values of Cronbach's alpha are used to test the consistency and reliability of data which is presented in table 1.

Table: 1 Reliability of Measurement

Constructs	Reliability (Alpha Value)	
Corporate Governance:	**0.7404**	
Transparency & Disclosure		0.793
Board Size		0.785
Auditing & Compliance of Law		0.644
Board Composition & Independency		0.740
Organizational Performance:	**0.7885**	
Profitability		0.841
Liquidity		0.763
Job Satisfaction		0.683
Employees' Commitment		0.867

Sources: SPSS output

Table 1 reflects the internal reliability for all scales used in this study. The table shows that the internal reliability for most of the constructs of all scales is greater than the cut-off level 0.7 of Nunally (1978). However, the result in the table shows that the Cronbach alpha for the construct of auditing & compliance of law and job satisfaction are 0.644 and 0.683 respectively. Although these values of Cronbach alpha are less than the cut-off level 0.7, they are acceptable as Mohapatra (1993); have accepted values for Cronbach alpha of 0.60, 0.55 and 0.62. As all the internal reliability of all scales are acceptable, the internal consistency of homogeneity of the measures is confirmed.

Table No. 2: Working Department and Academic Qualification of Respondents Cross Tabulation

	Academic Qualification				Total	%
Working Department	Bachelor	%	Master degree and above	%		
Customer Service Department	30	17.14	18	10.28	48	27.42
Credit Department	16	9.14	12	6.86	28	16.00
Operation Department	17	9.72	18	10.28	35	20.00
Remittance Department	20	11.43	14	8.00	34	19.43
Human Resource Department	8	4.58	12	6.86	20	11.44
Others Department	3	1.71	7	4.00	10	5.71
Total	94	53.72	81	46.28	175	100

Source: Survey, 2020

Table 2 shows that respondent's qualification and their working department in their respective banks. It is found that majority (27.42%) of respondents are from customer service department among them 17.14% respondents has bachelor degree and 10.28% respondents has master degree. Respondents are equal from operation and remittance department (20% and 19.43%) among them 11.43% respondents from remittance has bachelor degree and 8% respondents has master degree, 9.72% respondents of operation department have bachelor degree and 10.28% respondents has master degree. It is found less respondents (11.44%) from human resource department among them 4.58% has bachelor degree and 6.86% has master degree. It is also found that the participation from other departments bank employee is least in this study.

4. Results and Analysis

This study justifies the relationship between corporate governance and bank performance. This section of study attempts to analyze data associated with different factors of corporate governance and bank performance. Descriptive statistics are used to explain responses of bankers about different factors, Correlation analysis to describe the relationship among the factors and regression analysis to state the effects of corporate governance on bank performance. Different tables are used to simplify the data presentations as shown below.

Table 3: Descriptive Statistics

S.N.	Variables	N	Mean	Std. Deviation
1	Transparency & Disclosure	175	4.20	.68
2	Board Size	175	4.35	.71
3	Auditing & Compliance of Law	175	4.07	.60
4	Board Composition & Independency	175	4.12	.51
5	Profitability	175	4.08	.59
6	Liquidity	175	4.01	.74
7	Job Satisfaction	175	4.02	.63
8	Employees' Commitment	175	4.32	.38

Sources: Survey, 2020

Table 3 shows that responses of respondents on state of whether their institutions practicing corporate governance in their organization or not. Table also includes banking staffs' responses towards their job commitment and job satisfaction as well as institutional profitability and liquidity position. The average mean value of transparency & disclosure is 4.20 which means that their banks are fairly showing the all the financial information to al the stakeholders. The average mean value of board size is 4.35 which shows that respondents are highly agreed on that their institution has optimum level of board size. The average mean value of auditing & compliance of law is 4.07 which indicate that their institutions are timely audited their financial data and information and properly follow the government rules and regulations. The average mean value of board composition and independency is 4.12 which mean that majority of respondents believed that their board has composition of different experts and they are independent to make the decision prompt for organizational benefits. Similarly, the average mean value of profitability is 4.08 which expresses that majority respondents believed that their bank's profitability is very good. The average mean value of liquidity is 4.01 which shows that respondent's banks are maintaining optimum level of liquidity on their banks to face any liquidity crisis. The average mean value of job satisfaction is 4.02 which indicate that respondents are satisfied with their present jobs. The average mean value employees' commitment is 4.32 and average standard deviation is 0.38 which displays that banking staffs are really committed towards their job. It is found that banking staffs are more committed towards their work and the practice of corporate governance in Nepalese banking institutions is satisfactory.

Table 4: Correlation among Components of Corporate Governance and Organizational Performance

Variables	Transparency & Disclosure	Board Size	Auditing & Compliance of Law	Board Composition & Independency	Financial performance	Non- financial Performance
Transparency & Disclosure	1					
Board Size	237	1				
Auditing & Compliance of Law	435	328	1			
Board Composition & Independency	347	276	354	1		
Financial Performance	.693**	.247**	.745**	.644**	1	
Non-financial Performance	.687**	.238**	.756**	.673**	335	1

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

Sources: SPSS Output

Table 4 shows value of Pearson's correlation coefficient between elements of corporate governance variables and financial and non-financial performance of bank. Table shows that auditing & compliance of law higher positive association (r= 0.745 and r= 0.756) with financial and non-financial performance of banks. Similarly, transparency & disclosure is correlated (r= 0.693 and r= 0.687) with financial and non-financial performance of banks. The table also disclose that weaker association (r= 0.247 and r= 0.238) between board size with financial and non-financial performance of banks which indicate that larger board size tends to slow the decision making in organization. Table also shows the positive correlation (r= 0.644 and r= 0.673) of board composition & independency with financial and non-financial performance of banks. The result indicates that all variables are positively related with organizational performance. Among given set of independent variables, transparency & disclosure and auditing & compliance of law have stronger positive relation with financial and non-financial performance of organization which implies that Nepalese bank's performance is positively related with level of corporate governance.

Regression Analysis

The regression analysis is conducted to discover the effect of corporate governance on organizational performance in banking institutions of Nepal. The organizational performance (financial and non-financial performance) is considered as the dependent variable and corporate governance (transparency & disclosure, board size, auditing & compliance of law and board size & independency) is considered as independent variable. Thus, mean aggregate score on corporate governance is regressed on the mean aggregate score of organizational performance. The beta coefficients provided the relative importance of various corporate governance aspect. The highest beta coefficient value of corporate governance aspect is expected to have highest influence on organizational performance, while the lower beta coefficient stands second in terms of relative significance and so on. The Regression results are shown in tables below.

Table 5: Summary of Regression model

Model		R	R Square	djusted R Square	Error of the Estimate	
		0.646[a]	.708	0.687	0.32626	
		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	205.881	1	204.648	156.16	0.000
	Residual	54.647	41	1.426		
	Total	260.528	42			

a. Dependent variable: Organizational Performance

b. Predictors: Constant, Transparency & Disclosure, Board Size, Auditing & Compliance of Law and Board Composition & Independency.

Source: SPSS Output

The study used F-statistics to establish the appropriateness of the regression model to give reliable results and F- significance value of p=0.000 was established. This indicates that the regression model has a less than 0.001 likelihood (probability) of providing a incorrect prediction. Table 5 shows adjusted R^2 value is 0.687 which indicates that corporate governance contributes 68.7% of the variation in the organizational performance.

Table 6: Regression Coefficients

Model		nstandardized Coefficients		Standardized Coefficients	T	Sig.
		B	Std. Error	Beta		
1	(Constant)	2.034	.362		5.614	.000
	Transparency & Disclosure	.485	.036	.312	4.764	.000
	Board Size	.092	.035	.172	2.613	.000
	Auditing & Compliance of Law	.548	.047	.109	1.440	.000
	Board Size & Independency	.342	.056	.109	1.429	.000

a. Dependent variable: Organizational performance Sources: SPSS Output

Table 6 shows that there is positive relationship between corporate governance and organizational performance in Nepalese banking institutions. The un-standardized regression coefficients show how every metric unit change in the independent variable, the dependent variable changes by x units. This implies that a unit increase in transparency & disclosure would lead to increase in organizational performance in Nepalese banking institution at a factor of 0.485. A unit increase in board size would influence organizational performance in Nepalese banking institutions by a unit of 0.092. Similarly, a unit increase in auditing and compliance of law would lead to increase in organizational performance in Nepalese banking institutions at a factor of 0.548. Likewise, a unit increase in board size & independency would lead organizational performance in Nepalese banking institutions by a unit of 0.342. The results further show that there is a significant relationship between corporate governance and organizational performance in Nepalese banking institutions as shown by the p value; *($p=0.000<0.05$).*

The equation, $Y = 2.034 + 0.485X_1 + 0.092X_2 + 0.548X_3 + 0.342X_4$.

In conclusion, transparency & disclosure and auditing & compliance of law has significant impact on organizational performance in Nepalese banking institutions.

5. Discussion and Conclusions

This study intends to explore the impact of corporate governance on organizational performance in Nepalese commercial banks. It discovered the role of corporate governance is indispensable and integral to ensure the organizational performance in Nepalese commercial banks supporting the study of Delima and Ragel (2017) stressed that the result of the corporate governance is highly admired in the financial institutions in Srilanka. Similarly, Okoye et al. (2020) asserted that governance in business entities strongly affects their financial performance and recommends maintaining optimum board size to minimize boardroom and conflicts. Finding of present study tells that the corporate governance has different impact on organizational performance; transparency & disclosure and auditing and compliance of law play a stronger role in making better organizational performance in commercial banks operating in Nepal which is similar with study of Katrodia (2010) which analyzed that disclosure and transparency are the key pillars of a corporate performance framework in banking industry; Ilyas and Rafiq (2012) found that the corporate governance has widespread role in organizational success, that means there is positive relation between corporate governance and organizational performance. This study found that board composition and independency of management has significantly influences the organizational performance in Nepalese banking industry which is supported by the study of Miles (2010) which shows that composition of different experts in the board and independency of director has effect on organizational performance. This study observed that positive association between dependent (organizational performance) and independent (corporate governance) variables; Noticing that analyzed factors under this study has the significant impact on organizational performance which is consistent with the study of Burak, Erdil and Altindag (2017) which concluded that there is a relationship between the corporate governance principles consisting of the variables of transparency, fairness, accountability, social awareness, independence and discipline and business performance. Similarly, Grace (2018) reveals that adoption of good corporate governance enhances organizations performance and higher performance is achieved when organizations adopt the various corporate governance dimensions together. Adebayo, Ibrahim and Yusuf (2014) discovered that the adoption of good corporate governance practices enhances transparency of company’s operations, ensures accountability and improves firm’s profitability, helping to protect the interest of the shareholders by aligning their interest with that of the managers; concluding that generally corporate governance has positive impact on all the performance indicators of an organization. This study will be significant to financial institutions in providing a basis for policy making, and in showing direction for management of these institutions, researchers and academicians. Financial institutions may use the findings of the study in designing proper corporate governance strategies. Academicians will also find the study useful in adding to the existing literature on corporate governance. Finally, the study concludes that there is still a considerable room for further research and further improvements since, this study is based on only seven factors of corporate governance for analysis though there are other factors also for analysis in Nepalese commercial banks. In addition, the study has identified and analyzed the significance of corporate governance in Nepalese banking industry.

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