Does Corporate Governance effect on Companies Financial Performance in Oman

Essia Ries Ahmed¹, Yasser A. Al-Rawi² & Marwan Abd-Rassol Hamoodi³
¹Karabuk University, Turkey,
²University of Anbar, Iraq,
³University of Anbar, Iraq
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Abstract

The main objective of this study to investigate the role of corporate governance on firm performance in Oman. This is a cross-sectional study with a quantitative approach. Sample size of 60 companies from three sectors (Financial, Industrial, Service) of the Muscat Stock Exchange (MSX) were selected, which are analyzed with PLS (SEM) 3.0 software. The findings showed that (audit committee independence, board composition, board size and, CEO-Duality) have negative and insignificant relationship with the company performance (ROA). This result indicates that corporate governance not influence on the financial performance Muscat Stock Exchange (MSX).

Keywords: Corporate Governance, Financial Performance

Table 1. The list of abbreviations

<table>
<thead>
<tr>
<th>Abbreviations</th>
<th>Abbreviations Meaning</th>
</tr>
</thead>
<tbody>
<tr>
<td>ROA</td>
<td>Return on Assets</td>
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<tr>
<td>ROE</td>
<td>Return on Equity</td>
</tr>
<tr>
<td>MCMA</td>
<td>Muscat Capital Market Authority</td>
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<td>MS</td>
<td>Securities Market</td>
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<td>CGS</td>
<td>Corporate Governance Standards</td>
</tr>
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<td>EM</td>
<td>Earnings Management</td>
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<tr>
<td>CG</td>
<td>Corporate Governance</td>
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<tr>
<td>GCC</td>
<td>Gulf Cooperation Council</td>
</tr>
<tr>
<td>ICG</td>
<td>Islamic corporate government</td>
</tr>
<tr>
<td>CED</td>
<td>Corporate Environment Disclosure</td>
</tr>
<tr>
<td>FP</td>
<td>Firm Presentation</td>
</tr>
<tr>
<td>DLLP</td>
<td>Discretionary Loan Loss Provisions</td>
</tr>
<tr>
<td>ACI</td>
<td>Audit Committee Independence</td>
</tr>
<tr>
<td>BC</td>
<td>Board Composition</td>
</tr>
<tr>
<td>BZ</td>
<td>Board Size</td>
</tr>
<tr>
<td>CEO-D</td>
<td>CEO-Duality</td>
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</table>
1. Introduction

In 1998, the Government of the Sultanate of Oman decided to begin addressing issues that ran in the capital market. Like, weak internal controls, lack of transparency, Interests and duties of the management boards. The Muscat Capital Market Authority (MCMA) set in 2002 new Corporate Governance Standards (CGS) for companies registered in the Securities Market (MS). At that time, Sultan Qaboos supplied a regal modification of the commercial companies’ law to strengthen of the firms and improve of directors’ boards (Dry, 2003). Concerning Corporate Governance (CG) towards the duties of the directors’ board members in the public joint stock firm, it is required first and foremost to study the corporate governance law (known as the Gulf Cooperation Council (GCC) issued in July 2015. The aim of the GCC is to deliver an adequate and ideal scope for CG in public joint-stock companies with regard to directing, organizing and supervising them, through a series of specific policies, processes and procedures.

Generally, countries with advanced economies and low economies have increased their interest in Communication with CG to improve their companies (Abushammala et al., 2015). The reason for this interest is that CG has a fundamental role in operating and controlling the organizations’ context (Alabdullah et al., 2016; Alabdullah 2018; Alfadhl & Alabdullah 2013). Moreover, corporate governance is one of the basic elements that determine the shape of the company’s system and its ability to withstand economic crises. Therefore, wise and leadership corporate governance contributes to developing a sustainable economy. By improving and raising the company’s performance. So is their contact to external capital (Sarbah & Xiao, 2015). The Cadbury (1992) report means corporate governance is “the organization by which it is made "Companies are commanded and controlled” (Yılmaz, 2018).

Oman is ranked first in the Gulf in terms of its use the corporate governance rules for companies existing in the Muscat Securities Market, or what is currently known as the Muscat Stock Exchange, and from here, the MCMA and the Regulatory Authority have made efforts to provide everything related to governance. In addition, the state focuses on independent members of the board of directors “the form of the audit committee”. Where the government recommends the formation of other committees in the management boards, require significant disclosure of related-party transactions. The catalyst aspect in corporate governance refers to non-financial business. Although the financial firms made clear the risk management test on the organization, as it was not properly monitored by corporate governance, but also by good business performance and the development of result creation. Additionally, there are procedural incentives for company existence and price making (Ahmed et al., 2018).

Good corporate governance rises its value because it affects for investors and shareholders in terms of the quality of its financial reports and the inside control system. This concern for the quality of corporate governance is elucidated by its presence in the financial and non-financial costs linked with the quality of corporate governance, like, the reputation of the auditor and director, the success of the manager, the inventory price and the company values (Amrah & Obaid, 2019). In broadside, to achieve the contribution to the current corporate governance works and payment management through the prominent disclosure of how and why corporate and Islamic corporate government (ICG) mechanisms may affect their earnings management (EM) practices (Elghuweel et al., 2017). Therefore, the issue of corporate governance has become an interesting subject before countries with developed economies and developing
countries, after they were showing to disasters and events such as deception and corporate failure. Several stock exchange and supervisory agencies have issued instructions for corporate governance devices and their expose.

Corporate governance helps companies to achieve both businesspersons and stakeholders’ access to their rights. Where companies large and small resort to corporate governance to solve their problems. Sultanate of Oman has seen some problems related to companies, for example, the National Rice Mills Company, the National Investment Company, as well as the holding company, and for this reason, many small companies have turned to governance to solve their problems. These companies were accused of "hiding information" and "weak internal controls". In some, there have been fraud lawsuits on the part of board members. In 1998, both inefficient directors and boards were subjected to a lot of commentary about weak stock values that caused a loss of stockholder sureness (Dry, 2003). Thus, the main goal of this study is to investigate the role of corporate governance on firm performance in Oman.

2. Literature review

In this part, we will concentrate on the past studies for the last five years. Where, most of these studies have found that there is an effect of corporate governance on the company’s management performance. For example, a study by Gerged et al., (2021) inspected whether interior corporate governance devices has a reasonable relationship between Corporate Environment Disclosure (CED) and Earnings Management (EM). The findings revealed that while the connection between CED and earnings operations is bad, the links between CG provisions EM are mixed in that they might have also abridged or augmented earnings operations in Jordan. Aslam et al., (2020) tries to examine the amount to which the internal corporate governance structure influences the performance of the Islamic conventional banking system in Pakistan. They found that internal corporate governance structure improved performance in the financial sector. The results were reached by the researchers are useful for the officials and supervisors to develop the available governance structure aimed at accomplishing improved performance in the financial sector.

Khanifah, et al., (2020) studied the influence of disclosure of corporate governance on the performance of banks through building corporate governance disclosure directory for ten Islamic banks working in Iran, Saudi Arabia and Malaysia. The results bringing evidence that Islamic banks have a higher level of disclosure of corporate governance logged advanced working presentation measured by Return on Assets (ROA). Otherwise, they concluded that financial presentation of Return on Equity (ROE) and Tobin's q “Tobin's q is the ratio between a physical asset's market value and its replacement value” are not related to the Sharia bank governance disclosure. Baatwah et al., (2020) described in this study a data set on mechanisms of corporate governance (CG) in Oman using individual and composite measures. They recommended the possibility of using these measurements to investigate the mechanisms of corporate governance in various business and market issues.

A study by Rehman & Hashim, (2019) about organizational fraud and accessibility to committees, regulatory directives, and sovereignty guidelines. The results of this study indicated that mature corporate governance has a significant direct impact on the police role of criminal accountability. Amrah & Obaid, (2019) attempted to link the quality of corporate governance and the quality of economic reports among the private and non-private companies in Oman. They conclude that the link between the effect of corporate governance and the
quality of financial reports is positive and necessary for both the full trial and non-family companies. Nevertheless, the link appears to be weakened for family firms. Al-Hadi et al., (2018) tried to study the combined effect of inflexible ties, in the form of an associate of the royal family on the board of directors, and corporate governance on market risk disclosures in the GCC for the period 2007 to 2011. They concluded that better corporate governance recovers transparency and can be used as an effective tool in curbing the potentially adverse influence of electorally connected board members on firms’ transparency.

Pillai & Al-Malkawi, (2018) attempted to investigate the influence of internal devices of corporate governance (CG) on Firm Presentation (FP) in the GCC countries. The consequences display that supremacy variables such as administration shareholdings, audit kind, panel size, business social accountability and leverage meaningfully touch the FP in majority of the countries in the GCC. Ben Zeineb & Mensi, (2018) have studied the impact of the corporate governance (CG) of Gulf Collaboration Council (GCC) Islamic banks (IBs) on competence and risk. The study found that application of CG structures are related with advanced levels of efficiency. In addition, it lets them to take higher risks to attain a high equal of efficiency. Furthermore, results have demonstrated that the bank’s efficiency and risks are positively correlated. Bilal et al., (2018) aimed to inspect the effect of interior audit on actual corporate governance in profitable banks registered on Muscat Securities Market (MSM) in Oman for 100 banks within the period of (2014-2016). They found that there is a significant association between internal audit and effective corporate governance. The object of Yilmaz, (2018) study is to examine the link between corporate governance and financial presentation by using the data of 61 Oman businesses operated on Muscat Securities Market. The results displayed are important outcomes among monetary proportions then features of corporate governance but the general association is weak in Oman context.

3. The relationship between Corporate Governance and financial Performance

In this part, the researchers try to find the relationship between Corporate Governance and financial Performance. Amrah & Obaid, (2019) found that there is a significant relationship between corporate governance and financial reports. Bilal, et al., (2018) found an important
relationship between interior audit and corporate governance. Elghuweel, (2015) stated that the examinations indicate that Omani companies have responded positively to the references in the Corporate Governance Act 2002. Pillai & Al-Malkawi, (2018) found that the variables of governance (e.g. audit kind, administration shareholdings, leverage meaningfully, corporate social accountability and, board size) touch the fiscal policy in mainstream of the GCC countries. As well as, Ben Zeineb & Mensi, (2018) discovered that there is a positive correlated between the bank's efficiency and risks.

The results observed by Mersni & Othman, (2016) show that optional advance loss provisions (DLLP) damagingly linked to board size and the being of an audit. Gerged et al., (2021) revealed that while the connection between CED and earnings operations is bad, but there is a good relationship between CG provisions and EM. As per Aslam, et al (2020), to accomplishing healthier performance in the financial sector, improved the current governance structure results are useful for the officials and watchdogs. Rehman & Hashim, (2019) concluded that mature corporate governance has a direct effect on the police role of criminal accountability. Yilmaz, (2018) stated that there is an important outcome between monetary proportions and features of corporate governance but in the Oman context in general, the association is weak. Alabdullah et al., (2019) tried to linked between corporate governance arena and new trends in monetary Industry from Islamic viewpoint, they concluded that it will be add a strength positive additional to the arena of corporate governance due to the important role of these arenas. While Ajili & Bouri, (2018) concluded that there is no relationship between the quality of corporate governance and monetary performance, which means that good corporate governance, has an insignificant correlation with the high performance of IBs in the GCC countries.

Sami et al., (2011) concluded that the corporate governance has a positive and meaningful related with firm performance and valuation. The result reached by Malik & Makhdoom, (2016) concluded that there is a strong optimistic relationship between corporate governance and firm performance. According to Danoshana & Ravivathani, (2019), corporate governance variables have positive effect on the company's performance, management size and, audit size. Nevertheless, it has a negative influence on the company's performance when the meeting is recurrence. The consequences of the study test by Buallay et al., (2017) designate that here is no important influence for corporate governance acceptance on companies operational and financial performance in the companies registered in the Saudi stock exchange. Findings by Zaheer, (2013) presented that superior board size positively touches the level of corporate governance revelation whereas CEO-Duality and board composition does not have important impact on level of disclosure. Thus, the hypothesis developed is:

\[ H1: \text{there is a positive relationship between Corporate Governance and financial Performance}. \]

4. Research Methodology

It is a cross-sectional study with a quantitative approach in which quantitative data were collected from secondary data. In this study, we have the dependent variable, which is the performance found in the companies' annual reports, also we have the independent variables and it is corporate governance. In this research, a size of sample 60 companies of 115 for different sectors was chose (twenty financial firms, twenty industrial firms, twenty service firms). From the yearly reports found in Muscat Stock Exchange (MSX). In this analysis, annual reports for the year 2020 were used. The reports have a wide scope for testing the financial performance. This study analyzed the data were gathered with (PLS SEM) approach.
Table 2: Population and Sampling Method

<table>
<thead>
<tr>
<th>Sector</th>
<th>Companies</th>
<th>Samples</th>
</tr>
</thead>
<tbody>
<tr>
<td>Industrial</td>
<td>40</td>
<td>20</td>
</tr>
<tr>
<td>Financial</td>
<td>34</td>
<td>20</td>
</tr>
<tr>
<td>Services</td>
<td>39</td>
<td>20</td>
</tr>
<tr>
<td>Mutual funds</td>
<td>2</td>
<td>0</td>
</tr>
<tr>
<td>Bonds-sukuk</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Total</td>
<td>115</td>
<td>60</td>
</tr>
</tbody>
</table>

This study used a variety of scales to measure the selected variables available in the quality of financial reports as shown in the below table:

Table 3: Variables Measurement

<table>
<thead>
<tr>
<th>Variable</th>
<th>Acronym</th>
<th>Measurement</th>
</tr>
</thead>
<tbody>
<tr>
<td>Independent variable</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Board Size</td>
<td>BS</td>
<td>Sum of broad members</td>
</tr>
<tr>
<td>Audit Committee</td>
<td>ACI</td>
<td>Sum of members of board Independent audit. Alabdullah, and Ahmed, (2020)</td>
</tr>
<tr>
<td>Independence</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Board composition</td>
<td>BC</td>
<td>Number of non-executive board members.</td>
</tr>
<tr>
<td>CEO Duality</td>
<td>CEO-D</td>
<td>Result 1 is given if the person has two positions, which are the position of CEO and member of the board of directors, and if he has only one position, then it is given 0 Said, Zainuddin, and Haron,(2009)</td>
</tr>
</tbody>
</table>

Dependent variable

| Return on Assets      | ROA     | Net profit/Total assets                                                   |

5. Result and Discussion

5.1 Results

The study suggested a three-step analytical procedure: first, the descriptive statistics was evaluated, followed by the discriminant validity, and finally hypothesis testing for relationships between variables.
5.1.1 Descriptive Statistics

Table 4 shows the results of the descriptive statistics variables, this study utilized company performance (ROA) as a dependent variable, the level of return on assets was 1.44%, which represents the average performance of the company, with a Standard-D of (2.71). In addition, the maximum and minimum value designated of the return on assets is (9.64%) and (3.49%) respectively. Furthermore, the descriptive independent variables analysis shows that the audit committee independence averaged (4.83%) with a Standard-D of (1.93); the board size averaged (8.23%) with a Standard-D of (1.67); the board composition averaged (6.78%) with a Standard-D of (2.00); CEO Duality averaged (0.73%) with Standard-D of (0.44).

Table 4: Descriptive Statistics of Variables

<table>
<thead>
<tr>
<th></th>
<th>Mean</th>
<th>Min</th>
<th>Max</th>
<th>Standard-D</th>
</tr>
</thead>
<tbody>
<tr>
<td>ROA</td>
<td>1.446</td>
<td>-3.490</td>
<td>9.640</td>
<td>2.713</td>
</tr>
<tr>
<td>ACI</td>
<td>4.833</td>
<td>2.000</td>
<td>10.000</td>
<td>1.934</td>
</tr>
<tr>
<td>BZ</td>
<td>8.233</td>
<td>4.000</td>
<td>13.000</td>
<td>1.677</td>
</tr>
<tr>
<td>BC</td>
<td>6.783</td>
<td>2.000</td>
<td>12.000</td>
<td>2.009</td>
</tr>
<tr>
<td>CEO-D</td>
<td>0.733</td>
<td>0.000</td>
<td>1.000</td>
<td>0.442</td>
</tr>
</tbody>
</table>

5.1.2 Discriminant Validity

In this section, Table 5 shows that the AVE values must have a high association level counting the other concepts. However, to deal with discriminant cogency, as stated by Fornell & Larcker (1981), the square root of apiece concept in its AVE has to be likened versus the concepts' associations with all other concepts.

Table 5: Discriminant validity of Fornell-Larcker Criterion (n=60)

<table>
<thead>
<tr>
<th></th>
<th>AUD-COM-IND</th>
<th>B-COM</th>
<th>BZ</th>
<th>CEO-D</th>
<th>ROA</th>
</tr>
</thead>
<tbody>
<tr>
<td>ACI</td>
<td>1.000</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>BC</td>
<td>0.287</td>
<td>1.000</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>BZ</td>
<td>0.511</td>
<td>0.411</td>
<td>1.000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>CEO-D</td>
<td>0.338</td>
<td>-0.159</td>
<td>0.286</td>
<td>1.000</td>
<td></td>
</tr>
<tr>
<td>ROA</td>
<td>0.041</td>
<td>0.034</td>
<td>0.051</td>
<td>-0.065</td>
<td>1.000</td>
</tr>
</tbody>
</table>

An evaluation of the structural model was carried out after examining the dimensions model and passing all standards. In this study, an examination of (R²) was done. The results show in table 6 that the value of endogenous variable of (R²) is (0.011), and 0.061 for (R Square Adjusted), suggesting that 1%, 6% of the variance in ROA can be clarified by the predictors (CEO Duality, Board composition, Audit committee independence and, Board size). Therefore, the present work highly meets the standard.

Table 6: Explanation of the Variance
5.1.3 Hypothesis Testing

Table 7 shows that all hypothesis testing were rejected in this study. Where, the results showed that (audit committee independence (ACI), board composition (BC), board size (BZ) and, CEO-Duality (CEO-D)) had negatively relationship with the company’s performance at “t = 0.313”, t = 0.150, t = 0.471 and, t = 0.654 respectively.

Table 7: Path Coefficients

<table>
<thead>
<tr>
<th></th>
<th>Original Sample</th>
<th>Sample mean</th>
<th>Standard Deviation</th>
<th>T Statistics (O/STDEV)</th>
<th>P Value</th>
<th>Result</th>
</tr>
</thead>
<tbody>
<tr>
<td>ACI -&gt; ROA</td>
<td>0.050</td>
<td>0.046</td>
<td>0.158</td>
<td>0.313</td>
<td>0.755</td>
<td>Rejected</td>
</tr>
<tr>
<td>BC -&gt; ROA</td>
<td>-0.023</td>
<td>-0.023</td>
<td>0.154</td>
<td>0.150</td>
<td>0.881</td>
<td>Rejected</td>
</tr>
<tr>
<td>BZ -&gt; ROA</td>
<td>0.065</td>
<td>0.070</td>
<td>0.138</td>
<td>0.471</td>
<td>0.638</td>
<td>Rejected</td>
</tr>
<tr>
<td>CEO-D -&gt; ROA</td>
<td>-0.104</td>
<td>-0.095</td>
<td>0.159</td>
<td>0.654</td>
<td>0.514</td>
<td>Rejected</td>
</tr>
</tbody>
</table>

Note: *** P < 0.001 (t >3.33), **p < 0.01 (t >2.33), *p < 0.05 (t >1.605)

5.2 Discussion

For any business to be successful, performance must be regular and on certain principles and laws. Governance is related to the performance of the company's success. When the company sets the foundations, standards and laws regulating this, this will be reflected in the company's performance in terms of fairness, business transparency, investor confidence, attracting stakeholders and everyone who contributes to and strengthens the management. As well as raising the level of efficiency. Here, the company controls the level of performance and success of its employees, so governance is very important in its performance when setting laws, oversight, etc. this study tries to investigate the extent to which the independent variable affected the dependent variables of the companies selected from the MSM.

Four variables affecting the performance of the company were selected (CEO duality, board composition, audit committee independence, and board size), the quantitative data were obtained from the MSM website for the year 2020, where 60 companies for various sectors were collected from a total of 115. Therefore, the goal of this examine is to understand and analyze the extent of an impact of company governance and company performance in the Sultanate of Oman. As the result of this research appeared that, no hypotheses are important. The outcome of this research is that board size and performance are correlated, but with a negative relationship.

In one of the hypotheses that reached by Danoshana & Ravivathani, (2019) which was mentioned previously in this study, we found agreement with the result that emerged with us, where they said on this topic: The board size of directors and the audit committee when meeting is recurrence will negatively affect the company’s performance. When the previous hypotheses were analyzed in Table 6, the result emerged P<0.05, t = 0.150. The bottom line is, the association among board formation and its performance is negatively and insignificant.

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Furthermore, Audit Independent Committee is a committee of the same status as a board of directors. In communal area governments made up of independent members with accountability for providing oversight of management practices in sector of governance. Finally, there is a negative relationship and insignificant among audit committee independence and performance. Where, a person holding two positions, for example, director of board and chief executive officer of the firm.

6. Conclusion

The objective of this study is to investigate the association between corporate governance and corporate performance of companies present in the Muscat Stock Exchange at the year 2022. This study used four independent variables (CEO duality, board composition, board size, and audit committee independence) in order to measure the effect of corporate governance on corporate performance (ROA). After analyzing the data, the results showed that no variables belonging to the companies selected were indicative. In addition, the results showed that the variables (CEO duality, board composition, board size, and audit committee independence) not support a hypothesis of this study at (p value 0.514, 0.881, 0.638 and, 0.755) respectively. Other researchers may not support the results of this study, but this does not mean weak governance in the Sultanate. Other companies in the Muscat Stock Exchange (MSX) may have good governance and support companies' performance for their growth and success.

7. Future Study

For the future study, this study urges researchers to inspect deeply relationship between corporate governance and its performance in terms of addition variables such as panel promise and prize for presence. In addition, leading complete research on the panel of directors, the audit group, the executive group, and the ownership construction that improves corporate governance practices.

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