

RELATIONSHIP OF CORPORATE GOVERNANCE WITH FIRM'S PERFORMANCE AND DIVIDEND PAYOUT: A LITERATURE REVIEW

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Abstract *The present study aims to find the research gap between corporate governance, firm performance, and dividend payout through available literature and develop future scope of the study. The study reviewed 100 research papers covering time from 1995 to 2016. The papers were classified and analyzed based on various approaches.*

The review of literature indicates that research work on area of corporate governance has increased after 2007-08 crises. The study reveals that the relationship of different variables of corporate governance with dividend payout and firm performance are mixed in nature. It also indicates that different countries have different socio-economic, cultural, political, and legal dimensions that in turn affect the governance regulations of any country. Present study classifies, summarizes, and analyzes the past literature and provides a comprehensive review on corporate governance mechanism, which may be helpful for future research in same area.

Keywords *Corporate Governance, Dividend Payout, Firm Performance, Literature Review*

INTRODUCTION

Corporate governance (hereafter CG) as a field of study has been rapidly growing, both inside and outside academic circles. In the academic field, it not only covers finance and economic, but also law, management, and accounting. This shows the interdisciplinary interest of researcher in field of CG. Over the past few years, "CG," as a key word in the abstract of more than 987 research papers on SSRN (Bebchuk & Weisbach, 2009), has been found to be present. This indicates increasing popularity and interest of CG as a field of study among researchers.

It has also received considerable attention from corporate sector to instill confidence in investors. Levine (2004) suggested that the CG in financial sectors is different from non-financial sectors due to its nature and regulation.

Numerous significant studies presented that adoption of good CG enhances the firms' performance (Klapper & Love, 2004). Based on the result of the studies and perception, a number of companies in developing countries are implementing CG practices. According to Claessens and Leaven (2005), a firm having weaker legal environment obtains less financing and invests less amounts in intangible assets. The rapidly increased research in field of CG sectors may be due to the financial crisis in Asia in the year 1997. This was somewhat blamed on CG issues and led to an urgent analysis to help and guide the reforms in CG sectors (Claessens & Fan, 2002).

CG issues are important in developing economies, because these countries don't have strong, long-established financial institution infrastructure to deal with CG problems (McGee, 2009) and firms faced more agency problems (Core *et al.*, 1999). Economic growth depends on the development of corporate sector, so the establishment and improvement of CG is a matter of growing concern for developing countries. External finance is very important for infrastructure development in developing countries. Good CG practices provide substitute for weak national governance quality (Nguyen & Reddy, 2015).

Previous studies focused on developed and economically emerging countries. In developed markets, the relation between CG variables has been widely analyzed but very little work has been done in thinly traded emerging markets (Javed & Iqbal, 2007). Non-financial sector has been getting inadequate attention. There has been dearth of research in Asian region, mainly in India. This paper presents the reviews of the previous studies related to the need of CG practices and its relationship with financial performance and dividend policy of firms.

CG MECHANISM

CG is promoting corporate fairness, trainability, accountability, and responsibility of the managers and directors towards different stakeholders of the company. It is regulating the corporate activities in such a manner

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where conflict between managers and shareholder can be minimized.

CG can be classified in two parts: internal mechanism and external mechanism (Aljifri & Moustafa, 2007; Nguyen *et al.*, 2015). Internal CG mechanism monitors, controls, and manages the activities and takes corporative action to accomplish firms' goal. It involves ownership structure, board structure, audit committee, executive compensation, and transparency disclosure (Rosenberg, 2003). The external CG mechanism involves market for corporate control, proxy fights, managerial labour markets, product market competition, and legal infrastructure (Dalwai *et al.*, 2015).

Numerous studies describe the importance of CG mechanism. It was found that CG mechanism influences the dividend policy of manufacturing firms (Batool & Javid, 2014). Mehran (1995) investigated the relationship of executive compensation structure and their ownership with firm performance. The study found that % of executive total compensation and % of share held by top management was positively related to firm performance. This suggested that large ownership of executive in firm played an active role in CG of the firm. Nguyen and Reddy (2015) also suggested that ownership concentration was an effective CG mechanism, which substitutes for the weak national governance quality.

During the financial crisis, 2007-2009, it was found that large managerial ownership was positively associated with performance of state-owned enterprises in China (Liu *et al.*, 2012). Many studies (Liu *et al.*, 2012; Mehran, 1995; Vov-Lilienfeld-Toal & Ruenzi, 2009) stated that large proportion of managerial ownership enhances the firm performance, which could be measured by ROA, ROE, and Tobin's Q. However, Sheikh and Khan (2008) indicated negative impact

of managerial ownership on firm performance. Zhang (2008) found negative relationship between managerial ownership and dividend payout. Other variables like board size and independent director was found to have a positive relationship with firm performance (Bokpin *et al.*, 2011; Isshaq *et al.*, 2009) and dividend payout in Kenya and Ghana (Abor and Fiador, 2013; Bokpin, 2011). Duztas (2008) suggested that board size and outside directors were important to enhance transparency in companies. It is important to understand that CG mechanisms influence firms' performance and dividend policy, according to time and environment of the individual firm and country.

REVIEW OF LITERATURE

CG and Firm Performance

In CG literature, performance is widely researched area (Srinivasan & Srinivasan, 2011). Several studies found a positive relationship between CG and firm performance. According to Bebchuk and Weisbach (2010), good governance and firm performance have a positive correlation. It has shown the link of good CG with improved firm performance either in term of profitability and rise in share price. In India, performance-related research indicated that CG is much helpful for making performance and market valuation (Klapper & Love, 2004). At the same time, other researches have failed to find a link, indicating that literature review presented the mixed results. Table 1 presents findings from previous studies indicating relationship between different CG mechanisms and firm performance.

Table 1: Literature Summary of CG and Firm Performance

Authors	Findings and Suggestion
Mehran (1995)	The % of executives' total compensation and the % of share held by top managers were positively related to firm performance.
Core <i>et al.</i> (1999)	Weaker governance structure has greater agency problems, same as the firm had greater agency problems; where CEO received greater compensation, but the firms with greater agency problems perform worse.
Carter <i>et al.</i> (2003)	Found significant positive relationships between the fractions of women or minorities on the board and firm value.
Nandelstadh and Rosrnberg(2003)	Firm with high level of CG had delivered greater stock return and exhibit higher ratio of cash flow to assets in comparison with the company with low level of CG.
Klapper and Love (2004)	Found average firm level governance was lower in countries with weaker legal system and firm level CG provisions matter more in countries with weak legal environments.
Chen <i>et al.</i> (2005)	Found negative relationship between CEO duality and performance, same as family ownership and financial performance.
Chen <i>et al.</i> (2005)	There was a negative relationship between direct government ownership and performance in Chines securities firms.
Brick <i>et al.</i> (2006)	Discovered that excess compensation both to the director and CEO of the firms was associated with negative firm performance.

Kyereboah-Coleman and Biekpe (2006)	Found mixed results concerning CG and various measure of performance in Non-Traditional Export (NTE) sector. The board composition and ownership structure had positive impact on firm's performance in NTE sector.
Niu (2006)	Found that CG quality was positively influence the return-earning association but negatively related to the level of abnormal accruals.
Aljifri and Moustafa (2007)	Institutional investors, board size and audit type had a non-significant impact on the firm performance; however, the government ownership had a significant impact.
Zeitun and Tian (2007)	Ownership structure had significant positive and government share had significant negative impact on accounting measure of performance return on assets.
Bhahat and Bolton (2008)	Not all categories of CG affected the corporate performance. The financial disclosure, shareholder right and remuneration affected the stock price.
Omran <i>et al.</i> (2008)	Ownership concentration in Arab corporations was negatively associated with legal protection. The large size firms operated their business in less open economic gained more profit in compare to other firms.
Ehikioya (2009)	CEO duality and more than one member on the board were found to have an adverse effect on firms' performance. The result also suggested that ownership concentration, firm size and leverage have positive impact on firm performance.
Isshaq <i>et al.</i> (2009)	Among the CG variables, only board size was statistically significantly related to share price.
Cunat <i>et al.</i> (2010)	Changes in internal CG of the firms generate performance improvement in long run in S&P firms.
Berthelot <i>et al.</i> (2010)	CG raking published by the market information intermediary related both the firm market value and accounting results.
Bokpin <i>et al.</i> (2011)	Negative significant relationship was found between board composition and corporate liquidity holding; positive relationship found between board size, financial leverage, firms size, profitability and corporate liquidity holdings.
Guo and Kumara (2012)	Board size and increasing number of non-executive directors in board has shown a negative relationship with firm performance. The director shareholdings and firm size had a positive impact on firm performance.
Li <i>et al.</i> , (2012)	Found a positive causal relationship between CG and measures of liquidity, and a strong positive impact of CG on firm valuation. The evidence demonstrated the important role of liquidity in improving CG and valuation.
Martin-Reyna and Duran-Encalada (2012)	Firms with family ownership adopted substantially different CG structure to non-family firms. The evidence suggested that these differentials ultimately impact upon firm performance.
Mollah <i>et al.</i> (2012)	The evidence reveals major ownership concentration ware destructive to firms' value and financial performance except minority shareholdings.
Alipour (2013)	State, family and individual ownership was negatively related to performance, and firms and institutional ownership were positively related with performance.
Al-Saidi and Al-Shammari (2013)	Board composition and CEO duality positively influenced bank performance while other board composition variables (e.g. board size and proportion of non-executive directors) negatively influenced the bank performance.
Dedu and Chitan (2013)	Internal CG index influenced negatively on banking performance.
Gupta and Sharma (2013)	In comparison with south Korea, India followed more stringent CG practices. The main difference lied in mandatory disclosure.
Kim <i>et al.</i> (2013)	Stockholder wealth, board of directors, audit committee, disclosure, and dividend policy were significantly related to corporate performance.
Leung and Cheng (2013)	The result revealed that remuneration of top executives and ownership of other large shareholders showed different effects on firm value in central and local state-controlled listed firms (SCLFs).
Yu (2013)	There was U-shaped relationship between state ownership and firm performance. It also has shown that Split Share Structure Reforms played a positive role in improving the relationship between state ownership and performance.
Al-Najjar and Belghitar (2014)	The evidence suggested that UK institution were effective in forcing firms to disgorge cash dividend. It positively affected cash dividend payment of firms.
Halder and Rao (2014)	Results have shown that there was a strong association between CG Index and the market performance of companies.

Prommin <i>et al.</i> (2014)	The regression analysis result has shown a positive relation between increasing governance quality and significantly improved liquidity.
Al-Saidi and Al-Shammari (2015)	Government and individuals (family) ownership influenced the financial performance of the firms but overall concentration ownership by large shareholders had no impact on firm performance.
ji <i>et al.</i> (2015)	Investigated the effect of CG and ownership structure on earnings quality of Chinese firms before and later of two important reforms: the code of CG in 2002 and split share structure reforms in 2005, and found that promulgation of the Code of Corporate Governance (CCG) in 2002 had a positive impact but the Split-share Structure Reforms (SSR) in 2005 had little impact on earning quality of Chinese listed firms.
Nguyen and Reddy (2015)	Ownership concentration had significantly strong and positive effect on performance of Vietnamese firms in comparison with Singapore. It also sported the argument that ownership concentration was an efficient CG mechanism, which can substitute for weak national governance quality.
Phung and Mishra (2015)	There was a convex relationship between ownership structure and firm performance.
Zagorchev and Goa (2015)	Financial institutions take extreme risk to increase the wealth of shareholder but that can increase the instability of financial system. The evidence has shown that higher values for governance components and better CG were associated with higher profitability.

CG and Dividend Payout

Firm's dividend payout policy plays a major part in curtailing agency costs arising from the conflicts between the management and firm's stakeholders (Mancinelli & Ozkan, 2006). Several studies described the relationship between CG and dividend payout. Firms having higher growth opportunity paid lesser dividend (Subramaniam & Devi, 2011); firms with managing directors also acting

as CEO and fraction of managers on the board were associated with lower dividend payout (Zhang, 2008). The owners-managers reacted to financial need and investment opportunities of the firms, and adjusted the dividend policy accordingly. However, firms paid regular dividend in countries where the government was much concerned for shareholders protection. Table 2 reports findings from the past literature related to CG and dividend payout. Table 3 presents summary and critical review of Indian papers.

Table 2: Literature Summary of CG and Dividend Payout

Authors	Findings and Suggestion
Gugler (2003)	Firms with state-controlled engaged in dividend smoothing, while firms with family-controlled did not. It was found that firms with low rate of growth opportunities optimally disgorged cash irrespective of who controls the firms.
Mitton (2004)	Firm level CG and country level investor protection was associated with higher dividend payout and capital can be allotted more efficiently.
Mehar (2005)	Companies started to pay dividends after a certain level of growth and retain it on their earlier stage.
Mancinelli and Ozkan (2006)	Firm paid lower dividend as the voting right of largest shareholder increased in Italian market.
Kowalewski (2007)	The result demonstrated that CG was an important determinant in explaining the dividend policy of listed companies in Poland.
Abdelsalam (2008)	Firms having higher return on equity and higher institutional ownership distribute higher level of dividend. There was no significant association between board composition and dividend decision or ratios.
Al-Najjar and Hussainey (2011)	There was a negative association between dividend payout and number of outside directors on the board of directors.
Sawicki (2009)	There was negative relationship between governance and dividends in pre-crisis period. On the other side, it implied strong positive relationship between governance indicators and dividends in post-crisis period.
Setia-Atmajaf (2010)	Independent directors played significant role in influencing firms' dividend policies, that's why Dividend Payout Ratio (DPR) was much higher due to the higher proportion of independent directors on family boards. It was also found that family controlled firms appeared higher levels of leverage and DPR in comparison to non-family controlled firms.
Shah <i>et al.</i> (2011)	There was potential association between ownership structure and dividend payout policy and it has shown a positive relationship between them.
Bokpin (2011)	Foreign ownership and board size had significant positive effect on dividend payment among the CG variables. The Inside ownership, board intensity, CEO duality and board independency had not significant relationship with dividend payments.

Authors	Findings and Suggestion
Subramaniam and Devi (2011)	High growth firms paid lesser dividend, and board size board composition did not influence the dividend policy of Malaysian firms.
Abor and Fiador (2013)	Result indicated positive and significant relationship between board composition and board size with dividend payout in Kenya and Ghana respectively. Dividend payout positively influenced by institutional ownership among South African and Kenyan Firms but in case of Nigerian firms, all CG measures has shown significantly negative effect on dividend payout.
Bradford <i>et al.</i> (2013)	Firms controlled by state pay higher dividends as compared with privately controlled firms.
Al-Najjar and Belgitar (2014)	The evidence suggested that UK institution were effective in forcing firms to pay cash dividend. It positively affected cash dividend payment of firms.
Batool and javid (2014)	There was a positive relationship between dividend yield and CG (variables like ownership structure, board composition, audit quality and shareholder right). It indicated that firms implementing CG strategies paid higher dividend.
Ashraf and Zheng (2015)	Bank, which conducted operation in strong minority shareholder protection countries, paid higher amount of dividend.
Benjamin and Zain (2015)	Board independency and board meeting frequency were negatively related with dividend payout. CG and dividend payout were substitutes in reducing agency costs.
Chauhan (2015)	Examined the effect of CG on dividend policy in India, after controlling the influence of other variables like firms' profitability, firms' leverage and firms' size on dividend policy of the firms. It was found that good GC practices have an impact on dividend payout.
Yarram and Dollery (2015)	Board independency and its size have significant positive effect on the dividend payout thus providing support for the agency cost view of dividend policy.
Al-Najjar and Kilincarslan (2016)	State and foreign ownership were associated with a less likelihood of paying dividends in Turkey. All the ownership variables had significantly negative impact on the amount of dividend payouts and dividend yield of ISE Firms.
Byoun <i>et al.</i> (2016)	Result revealed that firms with gender/racial diversity in their board were pay more dividends in compare to firms with non-diverse boards.
Firth <i>et al.</i> (2016)	Mutual fund ownership influenced firms to pay higher cash dividend. It was more in firms controlled by state and regional government and in firms with higher free cash flows.

Table 3: Summary and Critical Review of Indian Papers

Author	Critical review
Halder and Rao (2014)	This study was examined impact of CG on financial performance taking Tobin's Q as the measures of market performance.
Aggarwal (2013)	This was an empirical study investigated impact of CG on firm performance of firm listed on S&P CNX Nifty 50. The period under study was two years 2010-2012 and sample size was 50 only, therefore not giving meaningful interpretation.
Author	Critical review
Joshi (2010)	This study measured the impact of CG on financial performance using data of only one year 2008. That is why result of study loses its importance.
Dwivedi and Jain (2005)	Study examined the impact of Board size and ownership structure on performance of Indian firm taking 340 large listed firms covering period of for year. However, study used only two variables, which not represent overall CG practices of firms.
Panchasara (2012)	Study investigated impact of CG disclosure practices on firm performance. Study took 18 banks as sample, therefore not giving meaningful interpretation.
Chauhan (2015)	This paper was examined the effect of CG on dividend policy in India taking sample of 30 listed companies on Bombay Stock Exchange (BSE).
Gupta and Sharma (2013)	This study examined the impact of CG practices on firm performance in Indian and South Korean firms taking 10 companies of each country.

RESEARCH METHODOLOGY

Present study is based on review of research papers on relationship of CG variables with financial performance and dividend payout of the firms. Literature is collected from various publishing groups like Emerald, Wiley Online Library, Elsevier, Science Direct, and many more. Study also included working papers and doctoral theses and research papers presented in conferences.

“Corporate Governance” as the key word is used to search the papers and hence selected papers published during the period 1995–2016. In the process of selection, preference is given to papers published after year 2000. The search have produced several research papers but the study has selected papers with key words “Corporate governance and firm performance”, and “Corporate governance and dividend payout” in the title and abstract of the papers.

Out of 100 papers, 85 papers are from 50 journals; five are working papers, four are presented in conference, and other six are doctoral thesis. These papers are classified and analyzed based on the year of the study, publication journal, themes of the study, countries where the study took place, methodology used and variable used.

ANALYSIS

There are numerous studies on CG, which are country specific or cross-boundary to examine the impact governance mechanism on dividend payout and firm performance. These researches initiative provides research and awareness on the big issues facing by the organizations and board of directors that includes CEO succession, proxy voting, executive compensation, transparency, and most important issue board governance. Studies also make valuable contribution to CG, which in turn encourages future development of the companies.

Year wise papers published during 1995 to 2016

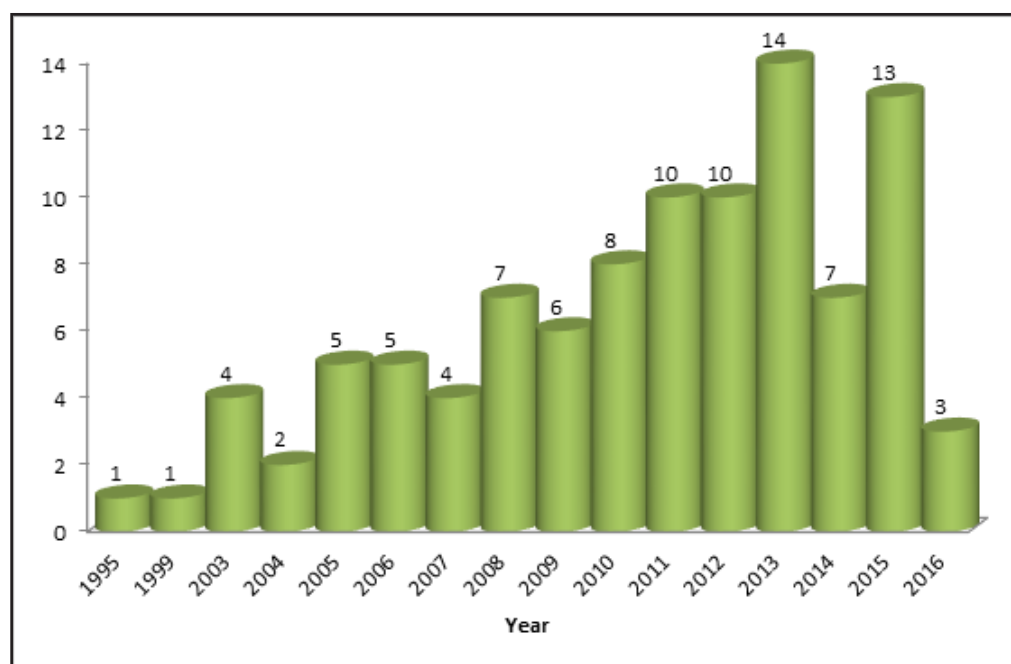


Fig. 1: Year Wise Papers Published

Researcher reviewed 100 papers published between 1995 and 2016 in various journals. It is observed that the number of papers published on CG is increasing every year. It can be seen in Figure 1 that after 2008 and 2009, the research in

field of CG is increased rapidly. World financial crisis may be one of the reasons for increasing importance of CG as a field of research.

Analysis of source of research papers

Figure 2 represents classification of the research papers according to different category. It can be concluded that

85% of research papers were collected from 50 journals. 5% papers were working paper and 4% having conference presented papers. Remaining 6% papers were collected through different website and other e-resources, which were reviewed in the present study.

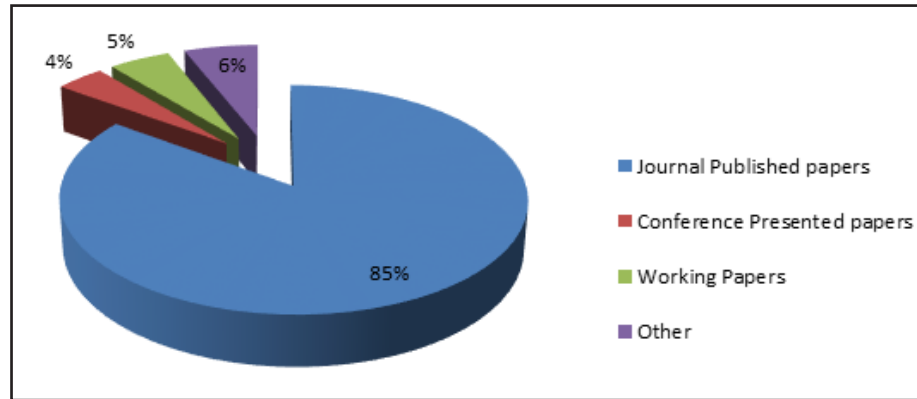


Fig. 2: Classification of Papers Base on Publication

Thematic Analysis

Figure 3 classified research papers based on the themes studied. Out of 100 papers, 71 papers were on performance as a theme. In the present study, the word “performance”

represents the accounting, operating, and market performance of the firm. The rest of 29 research papers were conduct by the researcher taking dividend payout as a theme. In these papers, “dividend payout” represents the policy of the firms regarding to pay dividend and not to pay dividend.

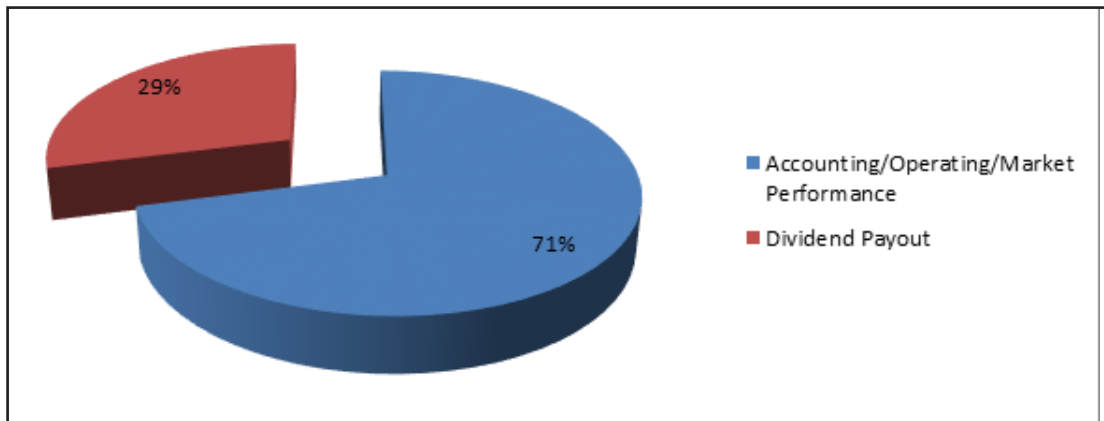


Fig. 3: Papers on Different Themes

Country Wise Distribution of Research Papers

Table 4 summarized country wise distribution of the research papers. It is observed that, individual contributions of the country are very less, except the USA that contributed 14% in total research. Some other country like China, India,

Pakistan, Malaysia, Australia, and Ghana contributed 5 to 7%. Figure 4 reveals that in 84% sample consists of only one country as the sample of the study. Only in 4%, it was two countries as a sample and made a comparative study between them. In five research papers, there were three to five countries as a sample and in rest of papers, they took more than five countries as samples of the study.

Table 4: Country wise distribution of papers

S. No. Name of the country (No. of Papers)		S. No. Name of the country (No. of Papers)	
1.	USA (14)	2.	China (7)
3.	India (6)	4.	Malaysia (5)
5.	Pakistan (5)	6.	Australia (4)
7.	Ghana (4)	8.	Iran (3)
9.	Turkey (3)	10.	Sri Lanka (3)
11.	Canada (2)	12.	Hong Kong (2)
13.	Japan (2)	14.	Kuwait (2)
15.	UK (2)	16.	Botswana (1)
17.	Costa Tics (1)	18.	Egypt (1)
19.	Finland (1)	20.	France (1)
21.	Italy (1)	22.	Indonesia (1)
23.	Jordan (1)	24.	Kenya (1)
25.	Korea (1)	26.	Mexico (1)
27.	New Zealand (1)	28.	Nigeria (1)
29.	Poland (1)	30.	Singapore (1)
31.	Taiwan (1)	32.	Thailand (1)
33.	Romania (1)	34.	UAE (1)
35.	Vietnam (1)	36.	Fiji and Solomon Islands (1)
37.	India And South Korea (1)	38.	Singapore and Vietnam1
39.	UK and Italy (1)	40.	Denmark, Finland, Norway and Sweden (1)
41.	Egypt, Jordan, Oman and Tunisia (1)	42.	Ghana, Nigeria, Kenyan and South African (1)
43.	Kenya , Tanzania , Uganda and Rwanda (1)	44.	Indonesia, Malaysia, Thailand, Hong Kong and Singapore (1)
45.	Sub-Saharan African countries (1)	46.	East Asian countries (1)
47.	15 Country Having Islamic banks (1)	48.	14 Emerging Country (1)
49.	19 Asian Country (1)	50.	30 countries (1)
51.	52 Countries (1)		

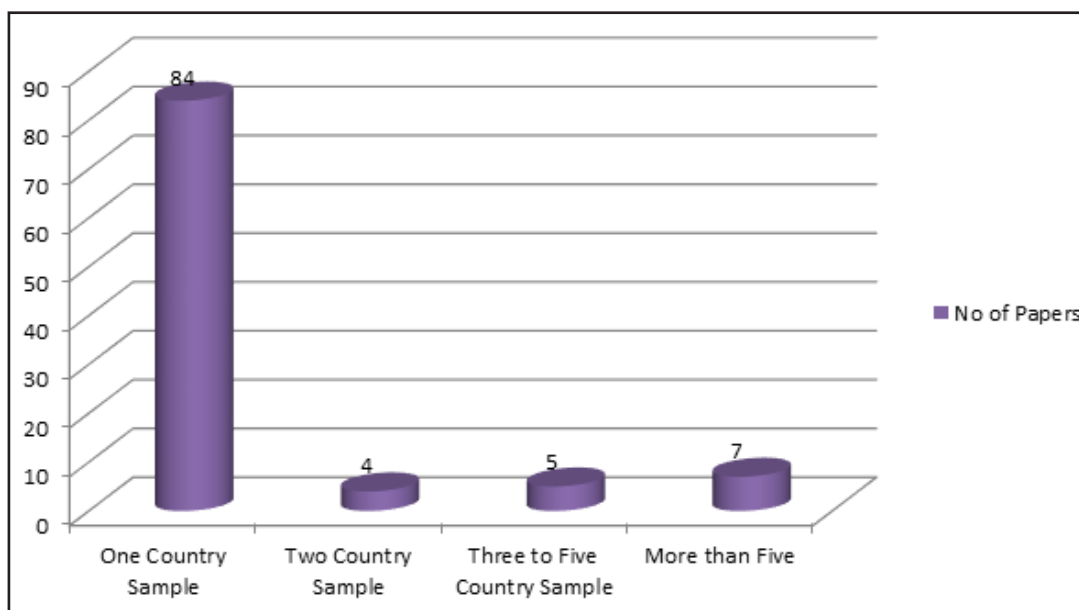


Fig. 4: Sample Countries

Econometric Tools used for Analysis

Research papers in the present study used various econometric tools for data analysis. It can be observed that mostly researcher have used regression analysis for data analysis. In limited studies where the researcher took dummy dependent variable, they used Logit and Tobit model to analyze the data. Other models like standard panel regression techniques, simultaneous panel regression analysis, etc., were also used in few studies.

Analysis of CG Variables

Various CG variables like board's structure and composition, ownership, and shareholders, remuneration

and compensation, committees, transparency, and disclosure have been used in the papers. From Figure 5, it can be inferred that 75% of studies the researcher used board structure and ownership concentration as the variables of CG. Only 20% of studies, researcher focused on the remuneration, different committee and transparency variables. In limited studies the researchers individually used ownership structure as a variables of CG. Out of these five variables, some other variables like corporate ethics, charter, national governance quality, etc., were also used in the research papers.

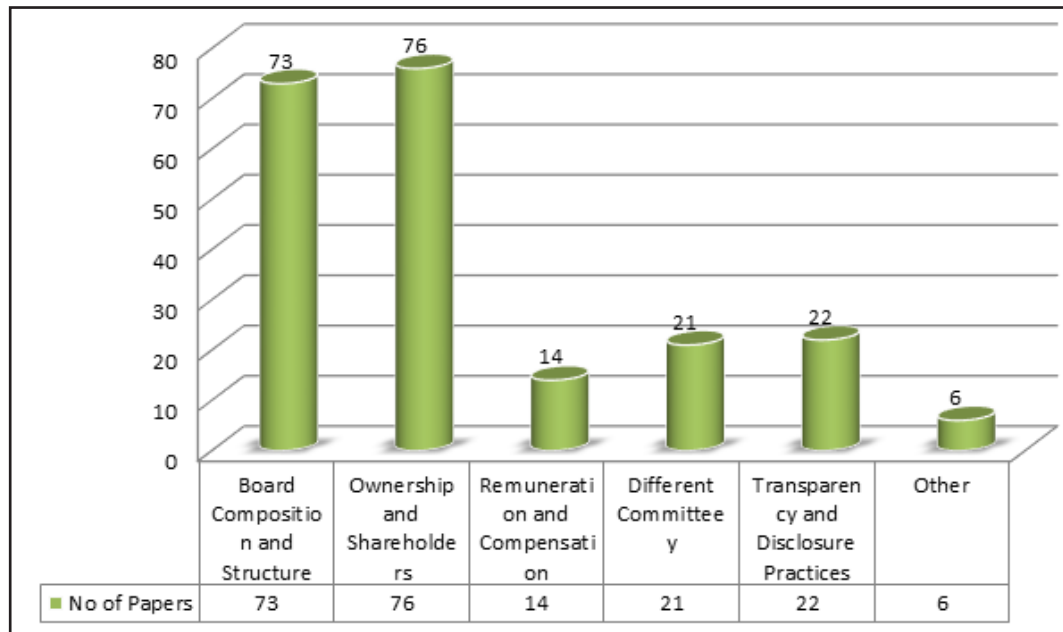


Fig. 5: Variables Repetition on Papers Basis

CONCLUSION

Present study is an attempt to analyze the literature of CG, and its relationship with dividend payout and financial performance. The study observed that CG research has gained popularity after 1997 world crisis but there has been significant rise after 2008 crisis.

According to Chhillar and Lellapalli (2015), it is apparent that in different circumstances and unique set of socio-economic, cultural, political, and legal dimension of the countries, the mechanism of CG like board structure and ownership pattern are different adopted by various countries. Due to this, impact of different mechanism of CG on dividend payout and firm performance are diverse in nature. For example Al-Najjar and Belghitar (2014), Setia-Atmajaf (2010), and Yarram and

Dollery (2015) found significant positive relation between size of independent directors in board and dividend payout.

On the other hand, Benjamin and Zain (2015) and Bokpin (2011) found negative relationship between these two variables. Srinivasan and Srinivasan (2011) describe the need for more empirical studies of CG in Indian context for development of theories that are embedded in ground realities in field of CG.

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