Board involvement in corporate performance: evidence from a developing country

Chaminda Wijethilake
Department of Management and Finance,
General Sir John Kotelawala Defence University, Ratmalana, Sri Lanka

Athula Ekanayake
Department of Management Studies, University of Peradeniya,
Peradeniya, Sri Lanka, and

Sujatha Perera
Department of Accounting and Corporate Governance,
Macquarie University, Sydney, Australia

Abstract

Purpose – The purpose of this paper is to provide insights into the understanding of the relationship between board involvement and corporate performance within the context of developing countries.

Design/methodology/approach – A number of aspects related to board involvement, including board’s shareholdings, frequency of board meetings, availability of independent board committees, board size, CEO duality, and CEO being a promoter, were examined in order to explore their influence on corporate performance measured in terms of earnings per share. The study mainly draws on agency theory, and is supplemented by resource dependence and stewardship theories. Multiple regression analysis is utilized to analyze the data gathered from a sample of 212 publicly listed companies in 20 industries in the Colombo Stock Exchange in Sri Lanka.

Findings – Among the aspects of board involvement considered, board’s shareholdings, board meetings frequency, independent committees, and CEO duality showed a positive influence on corporate performance. However, two other aspects, namely CEO being a promoter, and the size of corporate boards showed a negative effect. The findings also suggest that the use of multiple theories, rather than depending on a single theory, is more effective in understanding the relationships examined in this study. Further, the study highlights the need to be cautious in utilizing the theories that are more applicable to matured western economies when analyzing issues relating to developing countries.

Originality/value – This study makes an original contribution to corporate governance literature by examining the relationship between board involvement and corporate performance in a developing country, namely Sri Lanka. The study also adds to the existing literature by utilizing multiple theories to examine the issue under investigation.

Keywords Sri Lanka, Corporate governance, Corporate performance, Board involvement

Paper type Research paper

Introduction

Effective corporate governance could be regarded as a key factor in safeguarding the interests of the shareholders of companies operating in the capital markets (Fama and Jensen, 1983). Among the widely used corporate governance mechanisms, the board of directors (BOD) is considered as a prime governance mechanism in companies where...
ownership is separated from management (Ekanayake et al., 2009). The BOD is held responsible for good corporate governance of a firm as it has a fiduciary duty to monitor the activities of managers and provide strategic direction to the company (Cadbury Report, 1992; Kim et al., 2009; Pugliese et al., 2009; The UK Corporate Governance Code, 2010; Zhang, 2010). It also plays a significant role for the betterment of other stakeholders. According to Leblanc and Gillies (2005), the nature of directors, their functions, and the level of their performance are important issues, not only for all shareholders, but to the society in general (pp. 50, 51).

The effectiveness of the BOD as a corporate governance mechanism depends on two factors, namely how its role is defined and the way it is structured (Cadbury Report, 1992; Carver, 2010; Gillan, 2006; The UK Corporate Governance Code, 2010). The board is expected to ensure managers’ goal-congruent behaviour, and report to the shareholders on its stewardship. For these purposes, the board is meant to meet regularly to discuss matters important for the company, perform checks and balances, and ensure that effective control systems are in place to avoid malpractice by managers and other employees. Additionally, the board sets the company’s strategic aims and provides the leadership to put them into effect. Having an appropriate mix of directors in the board is important in fulfilling these tasks. Cadbury Report (1992) recommends the inclusion of executive directors who possess necessary qualifications and knowledge of the business, and non-executive directors who can bring a broader view of the activities of the company.

Duties and responsibilities of the BOD have been examined widely in corporate governance research in a variety of disciplinary areas. Despite the likely influence of BOD’s active participation in non-routine decisions as well as resource allocation decisions on long-term corporate strategies (Judge and Zeithaml, 1992), only limited attention has been paid to examine the impact of BOD involvement on organizational performance. Notable contributions to the literature in this area include Johnson et al. (1993) who examined the impact of board involvement in firm restructuring process, and Siciliano (1996) who focused on the relationship between board involvement and strategy formulation. The existing governance research also suggests various BOD-related characteristics including board independence, board composition, and compensation as good predictors of boardroom behaviour (e.g. Hillman et al., 2008). The literature, however, does not specifically examine the effect of board involvement, such as board participation in corporate activities, board’s personal commitment and relationships on corporate performance, particularly in relation to developing economies.

Although there has been numerous studies on corporate governance, more specifically on the role of BOD in corporate governance, universal applicability of the findings and conclusions of such studies is questionable due to varying contextual factors pertaining to research settings, such as national diversity, status of economies, political stability, institutional constraints, and cultural backgrounds (Carver, 2010). In particular, due to their different contextual characteristics, developing countries are likely to experience issues that may not be prevalent in developed countries. For instance, research findings reveal inefficient board involvement as a key factor that adversely affect investor trust and capital market interests in companies in developing countries (Chen et al., 2011; Phan, 2001; Ramdani and Witteloostuijn, 2010; Reed, 2002; Van Essen et al., 2012). Some researchers have even suggested that Asian firms do not follow the “good governance” prescriptions for BOD (e.g. Van Essen et al., 2012).

Our study aims to examine the role of board involvement in corporate performance in companies listed in the Colombo Stock Exchange (CSE) in Sri Lanka. Economic
indicators of Sri Lanka show a rapid growth since 2009, after the long standing civil war which had grave consequences on the economic development of the country. This study therefore is timely and would have important implications for Sri Lanka. Furthermore, studies on factors that assist economic development through capital markets in emerging economies could make a significant contribution to such economies (e.g. Li and Nair, 2009). The findings of this study also could be utilized in strengthening corporate governance in such countries, which in turn would have implication for their long-term sustainable development goals. Additionally, this study could contribute to the literature by providing new insights into the issues related to the board involvement in different institutional and environmental settings. A number of scholars (e.g. Carpenter and Westphal, 2001; Gibbs, 1993; Ruigrok et al., 2006; Siciliano, 1996) have highlighted the need for further research on board involvement in assessing the institutional and economic impact of various environmental constraints, and this study makes a contribution in this regard.

The remainder of the paper is structured as follows. The section that follows provides an overview of the institutional and regulatory framework that governs corporate governance in Sri Lanka. The third describes the theoretical approach adopted in this study and develops the research hypotheses tested. The fourth section outlines the research method, followed by the presentation of results of the study in the fifth section. The sixth section provides a discussion and conclusions of the study.

The institutional and regulatory framework that governs corporate governance in Sri Lanka

The corporate governance regulations applicable to listed companies in the CSE in Sri Lanka are governed by the Securities and Exchange Commission (SEC) and the CSE. In addition, effective from 2008, corporate governance of banks in the country is guided by a mandatory code of corporate governance issued by the Central Bank of Sri Lanka[1].

The SEC was established under the Securities and Exchange Commission of Sri Lanka Act (No. 36) of 1987 in order to govern the capital market in Sri Lanka. It has issued a number of regulations and guidelines related to corporate governance for listed companies. The guidelines that the SEC issued in 2008 contain provisions on the appointment of external auditors. Those provisions require rotating the engagement audit partner at least once every five years, and prohibit conducting non-audit services. Such guidelines are designed mainly to ensure auditors’ independence.

The SEC also partnered with the Chartered Accountants of Sri Lanka and issued its latest code of best practice on corporate governance in 2008. This code is intended for adoption by listed companies on “if not why not” basis. It has two main sections namely the company and the shareholders. The former provides guidelines on the responsibilities of the board. For instance, according to these guidelines the board should meet at least once in every quarter of a financial year. The code also promotes the division of the posts of the chairperson and the chief executive officer, and a balance between executive and non-executive directors in the board. Further, the board committees, such as the nomination committee, the remuneration committee, and the audit committee, are required to form exclusively of non-executive directors, and in some cases (e.g. audit committee), of independent directors. The criteria to determine “independence” of the non-executive directors are also laid down in the code. The latter requires the institutional investors to make considered use of their votes, and all the shareholders to participate in general meetings of companies and exercise their voting rights.
Nevertheless, not all corporate governance guidelines issued by the SEC were mandatory. A survey conducted by the SEC in relation to the audit committees of listed companies in Sri Lanka in 2005 revealed that a significant number of the listed companies (38 per cent) that responded did not have an audit committee (Securities and Exchange Commission of Sri Lanka (SEC), 2005). It also revealed substantial variations in the composition and function of the audit committees. For example, although companies had independent/non-executive directors in their audit committees, a substantial number of companies (56 per cent) had not appointed an independent/non-executive director as the chairperson of the audit committee (SEC, 2005).

To address this limitation, effective from 2006, additional rules of corporate governance were developed and incorporated in the listing rules of the CSE for mandatory compliance by companies listed on the CSE.

The listing rules of the CSE on corporate governance for listed companies specify the minimum number of non-executive directors (two, or one-third of the total number of directors, whichever is higher), the minimum number of independent directors (two, or one-third of the non-executive directors, whichever is higher), the criteria to determine “independence”, and the minimum requirements to be met by listed companies in the formation of remuneration and audit committees. Additionally, the listing rules require immediate disclosure of information such as any changes to the controls, directors, company secretary, and auditors. Such requirements of the SEC and the CSE are aimed at facilitating good corporate governance of listed companies in Sri Lanka.

Theoretical background and hypotheses

Although agency theory has been predominantly used in the corporate governance literature, stewardship and resource dependence theories have also been used widely to explain the behavior of BOD (Hillman and Dalziel, 2003; Muth and Donaldson, 1998). Rather than relying on a single theory to help understand the complex relationships examined in this study, this paper draws on multiple theories, namely agency, stewardship, and resource dependence theories. The current study aims to advance the theoretical implications of such perspectives by analyzing evidence from a developing country.

Agency theory, which is widely used in research on BOD (Dalton et al., 2007; Johnson et al., 1996), argues that owners of firms appoint managers to play a monitoring role on behalf of them to ensure that employees assist in achieving the goals of the organization. It also argues that to gain agent’s (manager’s) commitment to achieve the goals set by the principal (owner) and to promote goal congruent behavior, agents need to be given additional incentives over and above his/her basic remuneration. Consistent with the agency argument, the existing literature on BOD suggests that members of the BOD are expected to play an active role in monitoring the actions of managers on behalf of the owners, and further, that they would be more motivated to take such an active role if they have some claim to the firm’s output, possibly through their share ownership (e.g. Johnson and Greening, 1999).

Resource dependence theory characterizes an organization as an open system dependent on contingencies in the external environment. Pfeffer and Salancik (1978) propose five options that firms can adopt to minimize environmental dependences, among which BOD is one such option. Accordingly, the BOD is regarded as a critical resource that assists a firm in minimizing environmental dependences. Drawing on resource dependence theory, Hillman et al. (2000) argues that the BOD is an essential resource needed to maximize corporate performance. In general, BOD is expected to
constitute a mix of individuals who would have the interest, expertise and/or authority in
the organization’s activities, and such board composition would help to minimize
environmental dependences and maximize corporate performance. An active BOD could
make a significant contribution to corporate performance not only through its ability and
willingness to monitor managers, but also “in bringing valued resources to the firm and
in serving as a source of advice and counsel for CEOs” (Daily et al., 2003, p. 275).

Adding sociological and psychological perspectives to corporate governance
applications, proponents of stewardship theory suggest subordinates as collectivists,
pro-organizational, and trustworthy, whose characteristics ultimately enhance corporate
performance (Davis et al., 1997; Muth and Donaldson, 1998). Consistent with the
stewardship theory, Anderson et al. (2007) find that boards are evolving towards a
more collaborative role with management. It appears that in contrast to seeing the
BOD primarily as a monitoring body as suggested in the agency theory, the BOD is
now seeing as an entity that seeks a balance between collaboration and monitoring.

Drawing on the three theoretical perspectives referred to above (namely agency,
resource dependence, and stewardship theories), the following subsections develop
a number of hypotheses in order to evaluate the BOD’s involvement in corporate
performance in a developing economy.

**Board shareholding**

BOD’s share ownership is regarded as an important governance feature. It indicates
the extent to which the board members would be motivated to carry out their
governance role effectively, for instance to monitor managers in order to reduce
agency costs (Carline et al., 2009). Drawing on agency theory it can be argued that
when BOD has a considerable amount of share ownership, the interests of the members
of the BOD are more likely to be aligned with those of the shareholders. On the
other hand, BOD with non-shareholding is likely to have limited motivation to
effectively monitor managers, leaving room for them to engage in dysfunctional
and goal-incongruent behaviour (Finkelstein and D’Aveni, 1994).

Similar to most developing countries, in the Sri Lankan business environment,
there is evidence to suggest that a substantial number of successful companies are
controlled by families or have a high level of family influence. This is mainly because
of the inclusion of family members with a high proportion of shareholding in the board
(Chen and Nowland, 2010; Jackling and Johl, 2009). Drawing on agency theory, we
propose that ownership concentration involving the members of the BOD not only
motivates but also influences their ability to take effective monitoring measures
leading to reduction of conflict of interests (Chen et al., 2011). The above argument
leads to the following hypothesis that will be tested in this study:

**H1.** Board’s shareholding has a positive impact on firm performance.

**Board meeting frequency**

Drawing on resource dependence theory, it can be argued that active BOD involvement
is an effective mechanism to enhance corporate performance due to the increased
resource provision that accompanies such involvement (see Hillman et al., 2009).
Frequency of board meetings has been a main parameter to measure BOD activities
(Jackling and Johl, 2009; Vafeas, 1999). Frequent board meetings would also enable
the BOD to perform its monitoring role effectively as they become more informed
and more close to the activities of the firm. Following the agency argument, it can also
be expected that frequent board meetings would not only reduce information
asymmetry, but also promote managers’ goal-directed behaviour. Consequently, such outcomes of meeting frequency would have a positive effect on corporate performance[2]. Both, agency and resource dependence, theories suggest board members to have unbiased boardroom communication practices with fair number of frequency of board meetings in order to minimize information asymmetry as well as to reduce external dependences. Hence, we propose the following hypothesis:

**H2.** Frequency of board meetings is positively related to firm performance.

**Independent board committees**

According to Pfeffer and Salancik (1978) BOD bring four benefits to firms: first, information in the form of advice and counsel; second, access to channels of information between the firm and environmental contingencies; third, preferential access to resources; and fourth, legitimacy. Firms are able to gain such benefits by having an active and involved BOD. One aspect of board involvement is the appointment of committees such as audit, remuneration, and nomination committees in the board. Following the Enron and WorldCom scandals in 2002 in the USA, a number of international laws and corporate governance guidelines recommend that such committees should consist of independent directors (Chiang and He, 2010; Hansen et al., 2009; Lander, 2004). Empirical evidence suggests that these committees have been useful in enhancing the level of corporate performance and governance of firms. For instance, Dionne and Triki (2005) reveal that the requirements of the NYSE corporate governance rules (2003) and the Sarbanes Oxley Act of 2002 (2002) on the audit committee size and its independence are beneficial to shareholders. Hillman et al. (2008) also suggest that board members’ contribution on a committee would improve their identification within a firm, ultimately leading to enhanced corporate performance. Furthermore, Adjaoud et al. (2007) argued that firms having independent audit, nominating, and compensation committees have positive economic values rather than accounting values. In Sri Lanka, the code of corporate governance by the Institute of Chartered Accountants of Sri Lanka (ICASL) in 2008 requires companies to have at least three independent board committees, namely audit, nomination, and compensation, in order to upgrade the transparency and accountability on such corporate matters. Hence, we propose the following hypothesis:

**H3.** The presence of independent board committees is positively associated with firm performance.

**Board size**

The relationship between board size and firm performance has been much debated over the years. Institutional proponents suggest that large board size is favourable because of its ability to bring more expertise (Judge and Zeithaml, 1992). Similarly, resource dependence theorists suggest that having a large board size would intensify the firm’s responses to uncertain environmental conditions (Hillman et al., 2009). However, there has been a number of counter arguments. Maintaining a large BOD is seen to hinder effective and efficient decision making of a firm, for instance due to difficulty in organizing meeting times that suits the members (Eisenberg et al., 1998; Yermack, 1996). The diversity within the board when there are too many members could create conflicts leading to distrust, hostility, and less motivation (Ruigrok et al., 2006). Other issues associated with large board size include less communication and coordination opportunities as well as decision-making delays (Golden and Zajac, 2001), difficulties encountered by CEOs in controlling large BODs (Jensen, 2010), and less growth opportunities (Denis et al., 1999).
In the Sri Lankan context, there are certain concerns with regard to the size of BOD. For instance, the limited availability of sufficient board members with diverse expertise, and the selection of independent and non-executive directors in accordance with the governance requirements have been major issues (Gugler et al., 2003; Reed, 2002). Such difficulties often lead to the selection of members who do not satisfy the selection criteria sufficiently. Likewise, in developing countries, board membership is regarded as a way of getting social recognition and often seen as a position that can be described as passive and decorative (Van den Berghe and Levrau, 2004). Consequently, a large BOD has a more likelihood of having members who do not have the ability and/or interest to make an effective contribution to corporate governance. Therefore, this study proposes the following hypothesis:

\[H4. \text{Board size is negatively associated with corporate performance.}\]

**CEO duality**

A situation where one person holds both CEO and chairperson of the BOD positions in a firm is described as CEO duality (Boyd, 1995; Finkelstein and D’Aveni, 1994). Agency and stewardship theories have been the two dominant theoretical perspectives that highlight the contradictory arguments on this issue. While the proponents of agency theory suggest that separating these two positions is preferable in order to reduce the potential conflicts of interest (Finkelstein and D’Aveni, 1994; Van den Berghe and Levrau, 2004), stewardship theory proponents suggest that integrating the two positions offers the CEO with unambiguous authority and unique leadership power over the corporate practices (Muth and Donaldson, 1998). It has also been found that the performance of the BOD is better when the CEO also holds the position of chairperson (Elsayed, 2010). Nevertheless, academic research findings on the relationship between CEO duality and corporate performance are not conclusive (Boyd, 1995; Dalton et al., 1998; Elsayed, 2010; Finkelstein and D’Aveni, 1994; Jackling and Johl, 2009).

The inconclusive nature of the findings on the effectiveness of CEO duality could be due to the influence of various contextual factors on this relationship. For instance, its applicability may vary with the characteristics of firms, such as the firm size, age, and ownership (Elsayed, 2010). Based on evidence from developing countries, Li and Tang (2010) found that CEO’s hubris, known as CEO’s exaggerated self-confidence, has a positive impact on risk taking when managerial discretion was strong. Moreover, Van Essen et al. (2012) proposed that Asian firms are more likely to adopt CEO duality as non-CEO duality could prevent CEO’s discretion and diminish their ability of having relational exchange. Considering the Asian corporate culture featured with hierarchical power delegation and family-oriented ownership structure, and also drawing on the stewardship perspective, this study proposes that CEO duality in developing countries such as Sri Lanka would enhance corporate performance. Hence, this study tests the following hypothesis:

\[H5. \text{CEO duality is positively associated with corporate performance.}\]

**CEO as promoter**

CEOs of public companies hold important responsibilities on behalf of the shareholders, and are appointed with great care based on their qualifications and experience. In practice, there are also possibilities of appointing family-related board members as CEOs (Finkelstein, 1992). This situation is known as CEO becomes a promoter (see Jackling and Johl, 2009). Based on the resource-dependence perspective,
the CEO’s appointment as a promoter can be regarded as a measure to bring valued resources to the firm (Hillman et al., 2000). Stewardship proponents also imply that CEO being a promoter would extend their interest, motivation, and trustworthiness to the betterment of the firm (Davis et al., 1997). In contrast, based on agency perceptive, it can be argued that CEO’s appointment based on family connections would not fulfil the specific qualities and characteristics that are expected from such a position in corporate governance practices (see Chen et al., 2011). However, in the context of developing countries, there is a tendency to appoint CEOs based on their family ties irrespective of qualifications and experience, which can ultimately cause “controlling-shareholder expropriation” (Chen et al., 2011). CEOs selected mainly based on family ties may not be in a position to perform as well as those selected based on qualifications and managerial experience. Further, CEOs appointed purely based on family ties may make decisions and take actions that could hinder the performance of the firm. Therefore, we propose the following hypothesis:

\[ H6. \text{CEO as a promoter is negatively associated with corporate performance.} \]

Methods
Sample, data, and analytical approach
Sample for the study was drawn from Sri Lankan publicly listed companies registered in the CSE in 2008/2009. This sample includes 212 firms, representing 90 per cent of the population. The balance 10 per cent accounts for firms which had not submitted financial reports, discontinued operations, and commenced business during that year. Data were collected from annual reports of the companies and databases published by the CSE such as Fact Book 2008 and Data Library 2009. We applied multiple regression analysis to test our hypothesis. Table I depicts the detail analysis of the study sample.

Dependent variable
We applied earnings per share (EPS) to measure corporate performance. EPS is widely used to assess corporate performance on board engagement settings (e.g. see Adjăaud et al., 2007; Iyengar and Zampelli, 2009), CEO, boards, power, and corporate performance (Fizel and Louie, 1990; Pearce and Zahra, 1991), financial distress and corporate governance (Dyck and Zingales, 2004; Elloumi and Gueyie, 2001). Previous accounting research (e.g. Stickel, 1990) has identified EPS as one of the dominant indicators to evaluate corporate performance.

Independent variables
The independent variables of this study are share ownership of the BOD, frequency of board meetings, board committees, board size, CEO duality, and CEO being a promoter. Ownership of the BOD was measured as a percentage of board’s shareholdings divided by firm’s total shareholdings (Carlisle et al., 2009; McKnight and Weir, 2009). Board activities were identified as the frequency of board meetings held within a particular financial year (Vafeas, 1999). Boards committees were recognized as the availability of independent audit, nomination, and remuneration committees (Reeb and Upadhyay, 2010). Board size was measured as the total of independent, non-executive, and executive directors representing in the board (Ramdani and Witteloostuijn, 2010). CEO duality is whether the CEO holds both the CEO and the chairperson positions of a firm (Finkelstein and D’Aveni, 1994). CEO duality is a binary variable: a non-family
CEO with duality was coded “1” while non-duality was coded “0” (see Boyd, 1995; Finkelstein and D’Aveni, 1994). CEO being a promoter is recognized when CEO is appointed as a family member of a firm (Jackling and Johl, 2009). In this study, CEO’s family participation is measured by the fact that he or she is a family member or a relative of the founder as identified in the CEO’s last name or family name (see Finkelstein, 1992). If the CEO was a family member, it was coded “1” otherwise “0”.

**Control variables**
Firm age and size, which reflected organizational maturity (Matta and Beamish, 2008), were calculated as the natural logarithm of a firm’s age from the establishment and the sales volume per financial year (Hilary and Hui, 2009). The calculated natural logarithm form is applied in order to reduce the Heteroscedasticity (see e.g. Finkelstein and D’Aveni, 1994). Firm slack was measured by firm’s leverage and current ratios. The former was calculated as long-term debt divided by total assets (Ahmed et al., 2006), while the latter was measured with current assets divided by current liabilities (Jaggi and Gul, 2001). We also controlled executive-level variables, such as management team, executive directors and CEO’s cross-membership, in order to avoid their influences on board involvements. Management team was identified as the functional-level heads, and executive directors were measured as the number of executive directors in the BOD. The number of executive directors was controlled in this study in order to avoid CEO’s membership influence on executive directors. Moreover, CEO cross-membership, measured by CEO’s multiple board membership in audit, nomination, and remuneration committees, was controlled to identify the absolute impact of independent board committees. Further, with the aim of identifying the significant effect of CEO duality on corporate performance, the study controlled the CEO family duality relationship. The study also controlled
auditor-Big 4 vs non-Big 4 to control the effect of auditing practice on corporate performance (Choi et al., 2008; Bonner et al., 1998). Finally, this study controlled five industry dummies categorized as: banking, finance, and investment; trading and services; plantations, hotels, and beverage; diversified holdings, land, and property; and manufacturing and constructions in order to avoid environmental uncertainty and industry influences, including rules and regulations, on firm performance (see Finkelstein and D’Aveni, 1994; Kim et al., 2009).

**Empirical results and findings**

Table I provides descriptive statistics for the frequency of board meetings and CEO duality. Although the average of the frequency of board meetings is 6.83 times per annum, it ranged from one to 25 (as shown in Table II). One reason behind this wide range is the regulatory requirements. For instance, banks are required to hold minimum 12 meetings a year, while other companies to have minimum of four meetings per annum[3]. However, it is apparent that some companies have not met even the minimum requirement as required by code of conduct. We analyzed the CEO duality in two terms; CEO family duality and CEO non-family duality. It is interesting to note that 43 per cent of the Sri Lankan listed companies reported family CEO duality, while only a 2.4 per cent reported non-family CEO duality. Table II provides descriptive statistics of the other operationalized variables. As per the table, average shareholding of the board members in publicly listed companies is 10 per cent, and as discussed in the hypothesis, the board size range between four and 15[4]. Furthermore, 52 per cent of CEOs have been appointed with family ties, as promoters. Table III shows the outcomes of the Pearson correlation analysis.

<table>
<thead>
<tr>
<th>Variables</th>
<th>Minimum</th>
<th>Maximum</th>
<th>Mean</th>
<th>SD</th>
</tr>
</thead>
<tbody>
<tr>
<td>Earnings per share (EPS)</td>
<td>−125.54</td>
<td>148</td>
<td>6.15</td>
<td>19.13</td>
</tr>
<tr>
<td>Return on capital employed (ROCE)</td>
<td>−44</td>
<td>50</td>
<td>0.0017</td>
<td>0.052</td>
</tr>
<tr>
<td>Firm age (years)</td>
<td>7</td>
<td>143</td>
<td>36.34</td>
<td>24.95</td>
</tr>
<tr>
<td>Firm size (LKR millions)</td>
<td>0.750</td>
<td>114,115</td>
<td>374</td>
<td>10,659</td>
</tr>
<tr>
<td>Current ratio (times)</td>
<td>0.10</td>
<td>97.65</td>
<td>3.64</td>
<td>9.73</td>
</tr>
<tr>
<td>Debt ratio (percentage)</td>
<td>−255</td>
<td>2,772.0</td>
<td>147.73</td>
<td>376.78</td>
</tr>
<tr>
<td>Management team (members)</td>
<td>4</td>
<td>57</td>
<td>15.10</td>
<td>7.99</td>
</tr>
<tr>
<td>Executives (members)</td>
<td>0</td>
<td>7</td>
<td>2.76</td>
<td>1.68</td>
</tr>
<tr>
<td>CEO cross-membership (dummy)</td>
<td>0</td>
<td>1</td>
<td>0.43</td>
<td>0.496</td>
</tr>
<tr>
<td>CEO family duality</td>
<td>0</td>
<td>1</td>
<td>0.44</td>
<td>0.497</td>
</tr>
<tr>
<td>Audit Big 4 vs non-Big 4</td>
<td>0</td>
<td>1</td>
<td>0.83</td>
<td>0.376</td>
</tr>
<tr>
<td>Industry_1(dummy)</td>
<td>0</td>
<td>1</td>
<td>0.17</td>
<td>0.380</td>
</tr>
<tr>
<td>Industry_2(dummy)</td>
<td>0</td>
<td>1</td>
<td>0.17</td>
<td>0.372</td>
</tr>
<tr>
<td>Industry_3(dummy)</td>
<td>0</td>
<td>1</td>
<td>0.32</td>
<td>0.468</td>
</tr>
<tr>
<td>Industry_4(dummy)</td>
<td>0</td>
<td>1</td>
<td>0.17</td>
<td>0.376</td>
</tr>
<tr>
<td>Industry_5(dummy)</td>
<td>0</td>
<td>1</td>
<td>0.17</td>
<td>0.376</td>
</tr>
<tr>
<td>Board ownership (%)</td>
<td>0.00</td>
<td>97.00</td>
<td>10.46</td>
<td>20.13</td>
</tr>
<tr>
<td>Freq of Board meetings (numbers)</td>
<td>1</td>
<td>25</td>
<td>6.83</td>
<td>3.27</td>
</tr>
<tr>
<td>Board committees (number)</td>
<td>0</td>
<td>3</td>
<td>1.58</td>
<td>0.848</td>
</tr>
<tr>
<td>Board size (members)</td>
<td>4</td>
<td>15</td>
<td>7.78</td>
<td>2.23</td>
</tr>
<tr>
<td>CEO non-family duality (dummy)</td>
<td>0</td>
<td>1</td>
<td>0.02</td>
<td>0.152</td>
</tr>
<tr>
<td>CEO promoter (dummy)</td>
<td>0</td>
<td>1</td>
<td>0.52</td>
<td>0.498</td>
</tr>
</tbody>
</table>

Table II. Descriptive statistics of variables
<table>
<thead>
<tr>
<th>Variables</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
<th>6</th>
<th>7</th>
<th>8</th>
<th>9</th>
<th>10</th>
<th>11</th>
<th>12</th>
<th>13</th>
<th>14</th>
<th>15</th>
<th>16</th>
<th>17</th>
<th>18</th>
<th>19</th>
<th>20</th>
<th>21</th>
</tr>
</thead>
<tbody>
<tr>
<td>Firm age (log)</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Firm size (log)</td>
<td>-0.14</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Current ratio</td>
<td>0.14</td>
<td>-0.24</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Debt ratio</td>
<td>-0.05</td>
<td>0.21</td>
<td>-0.05</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Management team</td>
<td>0.07</td>
<td>0.19</td>
<td>-0.07</td>
<td>0.33</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Executives</td>
<td>0.10</td>
<td>0.06</td>
<td>-0.05</td>
<td>-0.01</td>
<td>0.05</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>CEO cross-membership</td>
<td>0.04</td>
<td>0.03</td>
<td>0.02</td>
<td>0.16</td>
<td>0.09</td>
<td>-0.08</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Audit Big 4 vs non-Big 4</td>
<td>-0.06</td>
<td>0.20</td>
<td>0.05</td>
<td>-0.11</td>
<td>0.02</td>
<td>-0.11</td>
<td>0.06</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>CEO family duality</td>
<td>0.13</td>
<td>-0.34</td>
<td>0.16</td>
<td>-0.14</td>
<td>-0.12</td>
<td>0.06</td>
<td>0.10</td>
<td>-0.08</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Industry_1(dummy)</td>
<td>-0.09</td>
<td>0.13</td>
<td>0.21</td>
<td>0.51</td>
<td>0.32</td>
<td>-0.10</td>
<td>0.20</td>
<td>-0.02</td>
<td>-0.18</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Industry_2(dummy)</td>
<td>0.13</td>
<td>-0.03</td>
<td>-0.09</td>
<td>-0.07</td>
<td>0.02</td>
<td>0.02</td>
<td>-0.03</td>
<td>-0.21</td>
<td>0.04</td>
<td>-0.20</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Industry_3(dummy)</td>
<td>-0.02</td>
<td>0.07</td>
<td>-0.05</td>
<td>-0.16</td>
<td>-0.22</td>
<td>0.11</td>
<td>-0.09</td>
<td>0.15</td>
<td>0.13</td>
<td>-0.32</td>
<td>-0.31</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Industry_4(dummy)</td>
<td>0.13</td>
<td>-0.29</td>
<td>-0.01</td>
<td>0.16</td>
<td>0.03</td>
<td>0.01</td>
<td>0.12</td>
<td>-0.03</td>
<td>0.11</td>
<td>-0.21</td>
<td>-0.20</td>
<td>-0.31</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Industry_5(dummy)</td>
<td>-0.14</td>
<td>0.10</td>
<td>-0.05</td>
<td>-0.10</td>
<td>-0.10</td>
<td>-0.07</td>
<td>-0.19</td>
<td>0.07</td>
<td>-0.12</td>
<td>-0.21</td>
<td>-0.20</td>
<td>-0.31</td>
<td>-0.21</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Board ownership</td>
<td>0.07</td>
<td>-0.07</td>
<td>-0.10</td>
<td>-0.04</td>
<td>-0.03</td>
<td>0.14</td>
<td>-0.06</td>
<td>-0.13</td>
<td>-0.09</td>
<td>-0.05</td>
<td>0.02</td>
<td>-0.04</td>
<td>0.07</td>
<td>0.02</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Board meetings</td>
<td>-0.04</td>
<td>0.25</td>
<td>-0.17</td>
<td>0.38</td>
<td>0.35</td>
<td>0.05</td>
<td>0.11</td>
<td>-0.06</td>
<td>-0.21</td>
<td>0.43</td>
<td>0.04</td>
<td>-0.29</td>
<td>-0.07</td>
<td>-0.04</td>
<td>0.14</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Board committees</td>
<td>0.06</td>
<td>0.30</td>
<td>-0.08</td>
<td>0.10</td>
<td>0.15</td>
<td>0.03</td>
<td>-0.14</td>
<td>0.12</td>
<td>-0.17</td>
<td>0.11</td>
<td>0.07</td>
<td>-0.15</td>
<td>-0.04</td>
<td>0.05</td>
<td>0.11</td>
<td>0.19</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Board size</td>
<td>-0.12</td>
<td>0.39</td>
<td>-0.24</td>
<td>0.23</td>
<td>0.22</td>
<td>0.26</td>
<td>-0.11</td>
<td>0.04</td>
<td>-0.19</td>
<td>0.15</td>
<td>-0.04</td>
<td>-0.02</td>
<td>-0.02</td>
<td>-0.02</td>
<td>-0.07</td>
<td>0.22</td>
<td>0.34</td>
<td>0.43</td>
<td>1</td>
<td></td>
<td></td>
</tr>
<tr>
<td>CEO non-family duality</td>
<td>0.08</td>
<td>-0.20</td>
<td>-0.03</td>
<td>0.17</td>
<td>0.00</td>
<td>-0.07</td>
<td>0.12</td>
<td>-0.18</td>
<td>0.18</td>
<td>-0.07</td>
<td>0.18</td>
<td>-0.11</td>
<td>0.01</td>
<td>0.01</td>
<td>-0.02</td>
<td>-0.05</td>
<td>-0.07</td>
<td>-0.07</td>
<td>-0.12</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>CEO promoter</td>
<td>0.17</td>
<td>-0.28</td>
<td>0.16</td>
<td>-0.24</td>
<td>-0.16</td>
<td>0.13</td>
<td>-0.04</td>
<td>-0.12</td>
<td>0.76</td>
<td>-0.23</td>
<td>0.00</td>
<td>0.19</td>
<td>0.12</td>
<td>-0.12</td>
<td>0.06</td>
<td>-0.17</td>
<td>-0.15</td>
<td>-0.08</td>
<td>-0.16</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>Earnings per share</td>
<td>0.16</td>
<td>0.01</td>
<td>0.16</td>
<td>-0.19</td>
<td>0.12</td>
<td>0.01</td>
<td>-0.03</td>
<td>0.07</td>
<td>0.06</td>
<td>0.03</td>
<td>0.10</td>
<td>-0.11</td>
<td>-0.02</td>
<td>0.02</td>
<td>0.12</td>
<td>0.13</td>
<td>0.15</td>
<td>-0.09</td>
<td>0.09</td>
<td>0.01</td>
<td>1</td>
</tr>
</tbody>
</table>

**Notes:** $n = 212$. Standardized correlation coefficients $\geq 0.14$ in the table were significant at $p < 0.05$ (two-tailed)
Regression analysis
Table IV shows the results of the regression analysis.

**H1:** proposed that board’s share ownership in a firm has a positive impact on corporate performance. As proposed, corporate performance shows a positive significant relationship ($\beta = 0.147, t = 2.156, p < 0.05$). Therefore, the study supports the **H1**.

**H2:** the hypothesis on the relationship between board activities and corporate performance proposed that frequency of board meetings has a positive significant influence on corporate performance. As hypothesized, the study found a positive and significant relationship ($\beta = 0.217, t = 2.746, p < 0.01$) supporting the **H2**.

**H3:** investigated the association between the availability of independent board committees and corporate performance. In line with the hypothesis, results of the regression analysis reveal a positive significant correlation ($\beta = 0.164, t = 2.209, p < 0.05$). This finding, therefore, supports **H3**.

**H4:** with regard to the relationship between the size of corporate boards and corporate performance, we hypothesized that board size is negatively correlated with corporate performance. As expected, supporting **H4**, corporate performance shows a negative significant relationship ($\beta = -0.230, t = -2.616, p < 0.05$).

<table>
<thead>
<tr>
<th>Variables</th>
<th>Predictive sign</th>
<th>Earnings per share (EPS)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Firm age (log)</td>
<td>+</td>
<td>0.072</td>
</tr>
<tr>
<td>Firm size (log)</td>
<td>+</td>
<td>0.127</td>
</tr>
<tr>
<td>Current ratio</td>
<td>+</td>
<td>0.161*</td>
</tr>
<tr>
<td>Debt ratio</td>
<td>-</td>
<td>-0.350***</td>
</tr>
<tr>
<td>Management team</td>
<td>+</td>
<td>0.154*</td>
</tr>
<tr>
<td>Executives</td>
<td>+</td>
<td>0.059</td>
</tr>
<tr>
<td>CEO cross-membership</td>
<td>-</td>
<td>-0.056</td>
</tr>
<tr>
<td>Auditor-Big 4 vs Non-Big 4</td>
<td>+</td>
<td>0.071</td>
</tr>
<tr>
<td>CEO family duality</td>
<td>+</td>
<td>0.108</td>
</tr>
<tr>
<td>Industry_1(dummy)</td>
<td>?</td>
<td>0.091</td>
</tr>
<tr>
<td>Industry_2(dummy)</td>
<td>?</td>
<td>0.050</td>
</tr>
<tr>
<td>Industry_3(dummy)</td>
<td>?</td>
<td>-0.006</td>
</tr>
<tr>
<td>Industry_4(dummy)</td>
<td>?</td>
<td>0.012</td>
</tr>
<tr>
<td>Board ownership</td>
<td>+</td>
<td>0.147*</td>
</tr>
<tr>
<td>Board meetings</td>
<td>+</td>
<td>0.217**</td>
</tr>
<tr>
<td>Board committees</td>
<td>+</td>
<td>0.164*</td>
</tr>
<tr>
<td>Board size</td>
<td>-</td>
<td>-0.230*</td>
</tr>
<tr>
<td>CEO non-family duality</td>
<td>+</td>
<td>0.160*</td>
</tr>
<tr>
<td>CEO promoter</td>
<td>-</td>
<td>-0.056</td>
</tr>
</tbody>
</table>

**R²** 25.1
**Adjusted R²** 17.7
**Model F** 3.383***
**F change** 4.370***

**Notes:** $n = 212$. Standardized coefficients are reported. *$p \leq 0.05$; **$p \leq 0.01$; ***$p \leq 0.001$
was on the relationship between CEO duality and corporate performance. Considering the counter arguments of the stewardship and the resource dependence theories, this study proposed that companies would benefit by having CEO duality. The EPS showed a positive significant association ($\beta = 0.160$, $t = 2.045$, $p < 0.05$), maintaining this hypothesis.

suggested that CEO appointed as a promoter can affect corporate performance negatively. Although the corporate performance demonstrated a negative effect ($\beta = -0.056$, $t = -0.477$), the findings are not statistically significant, hence the $H6$ is not supported.

Robustness of findings
In the analysis, this study employed both firm and executive-level control variables in order to assure the validity of the findings. The $R^2$ is 25 per cent and adjusted $R^2$ is 18 per cent showing a reasonable explanatory power of the model. All control variables also depict similar predictive signs while current ratio, debt ratio, and top management team revealed a significant association. This study assessed the Variance Inflation Factor in order to determine the multicollinearity among independent variables (e.g. Tihanyi et al., 2003). The results confirm that there is no multicollinearity effect among independent variables. The recorded maximum value is 3.5, which is below the accepted norm of 4.

Discussion and conclusion
The aim of this paper is to examine the relationship between board involvement and corporate performance in publicly listed companies in a developing country. Using multiple regression analysis, the study tested six hypotheses developed by drawing on agency, stewardship and resource dependence theories. Data to test the hypotheses were gathered from companies listed in the CSE in Sri Lanka. The study supports five of the six hypotheses. While the results show that share ownership, frequency of meetings, board committees, board size, and CEO duality are significantly associated with corporate performance, the study did not find significant results to support hypothesis six (i.e. the negative relationship between CEO as a promoter and corporate performance).

Consistent with the agency argument the study found that the BOD’s shareholding is positively related to corporate performance. In developing countries, particularly in Asian countries such as Sri Lanka, there is a high level of family ownership in publicly listed companies allowing family-related board members to acquire a significant portion of share holdings (Claessens et al., 2000). Our study shows that such shareholdings in turn increase the board’s interest towards the growth of the firm.

Existing research (e.g. Jackling and Johl, 2009) demonstrate conflicting views on the relationship between frequency of board meetings and firm performance. However, drawing on agency and resource dependence theories, we argued that the level of board activities is likely to be positively associated with firm performance, and found support for that argument.

Following agency and resource dependence views, we argued that the availability of independent board committees is positively associated with corporate performance, and this study supported this argument. Further, following resource dependence theory, we expected a negative association between board size and firm performance. The
relationship between board size and firm performance has been much debated due to inconsistent findings of studies conducted in the Asian region. For instance, Japanese firms depict a very strong negative impact while firms in Thailand, Hong Kong, and India show a positive significant association (Jackling and Johl, 2009; Van Essen et al., 2012). In line with our hypothesis, we found a negative association between board size and firm performance. This finding is consistent with prior studies, such as Ruigrok et al. (2006) and Yermack (1996), which concluded that large board size has a negative impact on firm performance.

Our study found strong support for the hypothesis that the CEO duality is positively associated with firm performance. In line with the notion of stewardship theory, our findings strongly suggest that integrating CEO-chairperson positions in the Sri Lankan context would enhance corporate performance. Our study found weak evidence for the hypothesis, developed based on agency theory, that the CEO as a promoter is negatively associated with firm performance. These negative insignificant findings do not support the suggestion that appointing the CEO based on family ties, despite the absence of required qualifications, could adversely affect corporate performance.

Overall, based on the aspects of board involvement examined in this study, it can be concluded that in developing countries such as Sri Lanka, board involvement in general leads to enhanced firm performance. While board involvement through share ownership, more frequent meetings, existence of board committees, and CEO duality are positively associated with firm performance, board size, and CEO as a promoter reveal a negative relationship. As a corporate governance mechanism, these findings in relation to board involvement have important practical implications. This study highlights the need for organizations to make a conscious effort to identify those aspects of board involvement that effectively assist corporate governance and enhance firm performance (e.g. board shareholding, frequent meetings, board committees, CEO duality). Organizations may be more careful in determining the board size and the composition of the board as it can negatively affect firm performance. Further, organizations need to pay more attention to the level of experience and qualifications when selecting CEOs as they seem to be as important as family ties. The findings of this study also offer useful insights to policy makers in the capital markets in Sri Lanka and other developing nations particularly in the Asian region. For example, policy makers may take into account the findings in relation to the aspects of board involvement when designing and implementing policies relevant to this specific corporate governance mechanism in such countries.

This paper makes a contribution to the literature by adopting multiple theories to understand the relationships examined in the study. While agency theory is the most widely used theoretical basis for a large number of corporate governance studies this study benefited by using additional theories to supplement agency theory as such approach allowed the development of clear and more convincing arguments in formulating the hypotheses tested in this study.

A main limitation of the study is that this research was conducted immediately after the introduction of new code of conduct for corporate governance by the ICASL in July 2008. Therefore, future studies are warranted to examine the different aspects of governance applications, and to compare the areas of developments or deviations. Future researchers may also replicate this study by using the same performance measure or by replacing it with other financial indicators such as ROA.
Notes

1. This code consists of principles of corporate governance relating to eight areas, namely responsibilities of the BOD, composition of the BOD, criteria to assess the fitness and propriety of directors, management functions delegated by the BOD, responsibilities and duality of the chairperson and the chief executive officer, BOD appointed committees, related party transactions, and disclosures.

2. There are also contradictory conclusions that intensity of board meetings frequency can be positively (e.g. Lipton and Lorsch, 1992) or negatively (e.g. Jensen, 2010) related to corporate performance. Vafeas (1999) also concluded that firms in which BODs are met more frequently have less market value compare to other firms.

3. The section 3 (1) (iii) of the corporate governance checklist for banking industry proposed by the IICASL mentions that “Check that the board has met regularly and held board meetings at least twelve times a year at approximately monthly intervals”. For other industries, the general rule is to have at least four (04) board meetings. The section A.1.1 of code of best practice (2008) of ICASL highlights that “The Board should meet regularly. Board meetings should be held at least once in every quarter of a financial year”.

4. In 2008/2009, 152 companies had minimum of seven or above board sheets, while 60 companies had six or less board of directors. One reason for having high number of board sheets (e.g. representing celebrities) may be to demonstrate the recognition or prestige of the company.

References


Further reading


About the authors

Chaminda Wijethilake is a Lecturer attached to the Department of Management and Finance, General Sir John Kotelawala Defence University, Sri Lanka. Chaminda Wijethilake is the corresponding author and can be contacted at: ubhayasiri-chaminda-banda.n@students.mq.edu.au

Dr Athula Ekanayake is a Senior Lecturer in the Department of Management Studies, the University of Peradeniya, Sri Lanka.

Sujatha Perera is an Honorary Fellow in the Department of Accounting and Corporate Governance at the Macquarie University, Sydney, Australia.

For instructions on how to order reprints of this article, please visit our website: www.emeraldgrouppublishing.com/licensing/reprints.htm

Or contact us for further details: permissions@emeraldinsight.com