



Salford Business School

**Corporate Governance: The Effect of Shariah Supervisory Board
on Malaysian Financial Institutions' Performance**

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DECLARATION

I declare that this thesis is the result of my own work and has not been submitted for any other degree at the University of Salford or any other institutions.

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ABSTRACT

This study explores the performance of Malaysian financial institutions and identifies the effectiveness of Shariah Supervisory Board (SSB) as a corporate governance mechanism. Despite the importance of the subject matter, little research has been carried out on the influence of Shariah Supervisory Board as a corporate governance mechanism on firm performance in Malaysia.

The conceptual framework describes how firms' performance is influenced by the presence and absence of SSB. In the framework, the corporate governance variables are Board size, number of non-executive directors, number of women directors, number of committees, number of board meetings, company age, SSB size, SSB women directors and qualification of the SSB directors. The dependent variable of firm performance is assessed by measuring financial performance ROA (Return on assets) and market value (Tobin's Q). This study primarily employs the agency theory to investigate the relationship between corporate governance and firm performance. It has been argued that board of directors; ownership concentration and managerial ownership are efficient corporate governance mechanisms for solving the agency problems between shareholders and management.

The study used the quantitative research method in which secondary data, comprising of the annual reports of the selected Malaysian financial institutions, was used to extract data. This study's sample of financial institutions'' was selected based on the DataStream database while data, related to governance-specific variables such as board-size, non-executive directors, women-directors, Shariah supervisory board-size and number of committees, was collected by hand, using the annual reports of each financial institution. To obtain quantitative measures of descriptive statistics, pair wise correlation and OLS (ordinary least square) STATA was used as a methodological tool to analyse the data.

The findings of this study revealed that good corporate governance practices have positive effects on firm performance. This study also finds that SSB characteristics have less influence on the Malaysian firm performance, so when it works in association with other board of directors, it results in better firm performance. This suggests a complimentary role of SSB.

Keywords: Corporate Governance, Shariah Supervisory Board, Financial Institutions, Malaysia, Board Size, SSB Size, Firm Size, Firm Performance

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Glossary of Terms

AAOIFI	Accounting and Auditing Organization for Islamic Financial Institution
AGM	Annual General Meeting
BNM	Bank Negara Malaysia
BCBS	Basel Committee on Banking Supervision
BOD	Board of Directors
CEO	Chief Executive Officer
IAIB	International Association of Islamic Banks
IFI	Islamic Financial Institutions
LIQD	Liquidity
MCCG	Malaysian Code of Corporate Governance
MYX	Malaysian Stock Exchange
NED	Non-Executive Director
OECD	Organisation for Economic Co-operation and Development
OLS	Ordinary Least Squares
ROA	Return on Assets
SSB	Shariah Supervisory Board

Chapter 1: Introduction

1.1 Background

Corporate governance relates to control, mechanisms strategies, distribution and accountability of power by which firms ensures balanced relationships among shareholders, related stakeholders and other interest groups. Since the past financial scandals, corporate governance has become an issue in developing economies and this has created demands for better corporate governance practices (Baydoun et al., 2013). Because of the significance of corporate governance in the business world, it has become a broadly discussed issue in all developed and developing countries. The general point of view of corporate governance among investors and organisations is that it influences and determines the performance of the firm to protect the interests of shareholders (Garcia-Torea et al., 2016). Thus, corporate governance has become an evolving topic around the world.

Several scholars and authors have studied the effect of corporate governance mechanisms on firm performance and they have found different outcomes from the studies. Some of the authors have found positive correlations between corporate governance and firm performance (Kiel and Nicholson, 2003; Haniffa and Hudaib, 2006; Jackling and Johl, 2009). To enhance the investment environment, improve firm performance, encourage economic development and establish investor rights, the practice of good corporate governance is required. It has also gained widespread fame in the stock-market economy (Adiloglu and Vuran, 2012). Most empirical studies have documented a positive relationship between corporate governance and corporate governance mechanisms, even though establishing the relationship between these

two was complicated (Bhagat and Bolton, 2008). Other studies have cited that corporate governance has less influence on firm performance (Hutchinson and Gul, 2003; Mashayekhi and Bazaz, 2008).

It has been widely studied by researchers that corporate governance plays a significant role in improving firm performance. For example, Chhaochharia and Grinstein (2007), Dey (2008) and Mishra and Mohanty (2014) have highlighted that a firm performance can be significantly influenced by its corporate governance rules and practices. However, little is known about the effect of SSB as a governance mechanism on firm performance of financial institutions in Malaysia. Therefore, the current study fills the gap to understand whether SSB is integrated or segmented with regular boards and if it affects firm performance.

Therefore, the current study aids the understanding of corporate governance practices with and without SSB and the impact of these practices on firm performance.

1.2 Motivation of the Study

This study is motivated by several considerations. Firstly, despite the importance of SSB being present in Islamic financial institutions, it has been found from the sample of this study that there are still some Islamic firms that have no in-house SSB. It has encouraged me to re-examine the reason behind the absence of SSB in those firms and also to find out if the SSB or other factors are affecting the performance of the firms. Secondly, the variations in the type of sample firms, markets, and sample periods used in prior studies motivate this study to further examine the relationship between governance mechanisms and firm performance.

1.3 Research Objectives and Research Questions

The aim of this study is to explore the extent of SSB as a corporate governance mechanism by analysing the implementation and practices of SSB in Malaysian financial institutions through the opinions and perceptions of participants and available documents. There are a number of objectives through which the purpose of the study will be achieved, which are as follows:

1. To investigate the extent of corporate governance effect on the performance of Malaysian financial institutions’.
2. To identify the similarities and differences between the performance of firms’ with SSB and firms’ without SSB within the scope and framework of this study.
3. To examine the reason for not having SSB in Islamic financial institutions even though it is a requirement.

This study seeks to answer the following research questions:

1. Is there a relationship between corporate governance mechanisms and the performance of Malaysian financial institutions’?
2. Is there any similarity and difference between the performances of firms’ with SSB and firms’ without SSB?
3. Is there any reason behind the absence of SSB in Islamic financial institutions despite the requirement?

1.4 Significance of the Study

The Malaysian setting is particularly interesting for a number of reasons, firstly this study might help to get a better understanding of corporate governance in terms of agency theory in Malaysian financial institutions and if there are any possible improvements needed to deal with it. Secondly, the findings of this study may benefit many other countries with similar cultural, political, economic and environmental situation. In addition, it will also help to benefit the researchers, regulators, academics, investors and decision makers and will also assist the policy makers to make better governance standards.

1.5 Research Scope and Limitation

The study focuses on the publicly listed financial institutions in Malaysia. The period of the study is 2012 - 2016 following the Malaysian Corporate Governance Code 2012 as the fundamental framework. Relevant data on financial information is collected from annual reports of the firms, Datastream and Malaysian financial market websites. Quantitative analysis is employed in the data analysis to examine the relationship between firms' performance and corporate governance variables.

Nevertheless, this study has some limitations. Unlisted companies are not included due to lack of information. The main source of data for this study is mostly from the annual reports and it is a requirement for this study to have complete data for each year. Therefore, survivorship bias is an inherent limitation of this study.

1.6 Dissertation Structure

The thesis comprises six chapters, commencing with Chapter 1 which introduces the topic and provides the background to the study as well as identifying gaps in the literature.

Chapter 2 provides the literature review part 1 on corporate governance practices and firm performance. Chapter 3 explains literature review part 2 on the Shariah Supervisory Board in Financial Institutions.

Chapter 4 explains the methodology of the study and includes the research hypotheses, the discussion of the variables used in the model for corporate governance and firm performance. It includes the data collection methods, measurement used and the conceptualisation and operationalisation of the hypothesis. The testing procedures employed to analyse the data used for the study are explained.

Chapter 5 discusses the results of the statistical analysis of the data. The descriptive statistics compare the corporate governance variables and the performance of Malaysian financial institutions'. Correlation is used to measure the strength of association and an analysis of variance tests the hypothesis of the study and explains the interaction between the corporate and firm performance variables. In addition, the importance of individual governance variables in affecting firm performance variables is also discussed. This chapter further provides empirical evidence to accept or reject the hypothesis of the study.

Chapter 6 presents the summary and conclusion of the study. In particular, it provides an overview of the analysis of the relationship between corporate governance practices and firm performance. It also discusses the limitations and suggestions for future research directions.

Chapter 2: Literature Review 1: Corporate Governance and Firm Performance

2.0 Introduction

Corporate governance is a modern management approach that has been at the forefront of discussions of the financial services in companies for decades. The dramatic rise of globalisation has brought changes in the structure of strategy, administration and management of a business and has left firms under pressure to expand in the international markets (Musteen et al., 2009). The importance of corporate governance continues to gain widespread prominence in the capital market and it has attracted the attention of the public as well as national and international firms with the effect of globalisation, firms valuation criteria and investors decision (Adiloglu et al., 2012). Corporate governance issues have caught the attention of most scholars and have been touched upon in many studies because of all these reasons.

2.1 Definition of Corporate Governance

The term corporate governance has recently become more popular from different perspectives such as regulators, professional bodies and academics. Furthermore, due to the rising concern of corporate fraud and fraudulent financial reporting, corporate governance became popular in both developed and developing economies. There is a considerable argument among researchers and scholars about the corporate governance definitions. With regard to the various definitions, researchers and scholars in either narrow or broad sense classify corporate governance definitions. The narrow perspective is based on satisfying the shareholders' interests. However, in a broad perspective, it is the extension of previous

definitions and is based on satisfying the interest of the stakeholders (i.e. employees, government, customers and suppliers) (Letza et al., 2004; Sternberg, 2004; Gillan, 2006).

The definition fundamentally relates to the epistemological assumptions involved (Gillan, 2006). Corporate governance, for instance, can be perceived from the viewpoint of the shareholders. From the perspective of the organisation, this is the main motivation to maximise value of control mechanisms to main business operations (Zingales, 1997). Corporate Governance deals with the ways in which suppliers of finance to corporations assure themselves of getting a return on their investment as stated by (Shleifer and Vishny, 1997). In case of corporate operations, it is normally not possible for principals in a modern public firm to be charged with responsibility, for this reason they entrust agents to supervise operations in their interests. As a result, due to the necessity of counteracting agency problems, corporate governance issues occur (Hart, 1995), and fundamentally from shareholders' attempts to protect themselves from the expropriation of their wealth as claimed by Shleifer and Vishny, 1997).

This broad explanation is based on the organizational context, which is way more general. In other words, the broad definition does not provide the required theoretical frameworks that can be established on the basis of testable hypotheses or relationships. Whereas agency theory is an extensively used framework to conceptualise the relationship between firm performance and organizational structure, which was stated by Denis and McConnell (2003) in terms of being an appearance of property rights in corporate governance by principals; any understanding of firm structure must be started with the provision that shareholders are the primes (i.e. owners) in the organization.

Nevertheless, the agency theory is employed by this study as the main theory to examine the relationship between corporate governance and firm performance. The interests of the shareholders with relation to the agency problem and the underlying target of value maximization are contracted by the agency theory. On the most primitive level, decreased agency problems contribute to escalating the share value and consequence of this positive performance. This slight conceptualisation prioritizes the interests of the shareholders, whose overarching interest is value maximization. As a result, the narrow explanation is more appropriate while it offers the direct connection between corporate governance and financial performance with a view to the objective of the thesis to analyse the impact of corporate governance on firm performance. In cooperation with the narrow definition of corporate governance and the agency theory portray theoretical justification for the association between corporate governance and firm performance and therefore allow the testable hypotheses on the different corporate governance mechanisms in terms of progressed financial performance.

2.2 Importance of Corporate Governance

The significance of corporate governance has escalated internationally in the last decades hence mobilisation of capital, trade liberalisation, arising financial markets, technological progression and financial crises. Corporate governance regarded as prime subject matter in the boardrooms of companies, amongst legislators and academics, and also considers it as an essential framework for companies by Claessens et al. (2000). Corporate governance becomes a vital assessment tool for investment choices as studies by Black (2001), Black et al. (2006), Selvaggi and Upton (2008) strongly support positive correlation between corporate governance behaviour and firms' performance. Similarly, when investors are in the decision making process, firstly they look at the implications of corporate governance and its

compliance first, with the advices and regulations. Therefore, corporate governance is an important element in the decision making of investment.

The principles of corporate governance are important and the degree of implementation of these principles and codes are critical to an effective corporate governance mechanism. These principles are not only to increase and protect shareholders' value but also to ensure an elimination of conflict of interest, the interests of all stakeholders are considered and enforcement of transparency and accountability function properly in the interests of not only shareholders but also other stakeholders.

According to Thorne et al. (2011), corporate governance focuses on the strategic-level of accountability and control leading to effective performance of all types of organisations. It is a balanced system that focuses on many corporate constituencies and perspectives such as proper resource allocation, delegation of power, decision-making authority and responsibility in accordance with strategic directions.

In the perspective of financial institutions, Clasessens (2003) considers that corporate governance plays an important role in determining firms' performance in respect of lowering cost of capital, ability to facilitate access to external finance, mitigate operational risk, improve performance and build a better relationship amongst the stakeholders. In this regard, a clear and detailed framework of corporate governance will stimulate the efficiency of financial institutions' resolving agency problems, avoiding unnecessary agency cost and leading towards better firm performance (Hart, 1995). Corporate governance requires financial organisations to be more transparent and ensure equality not only to shareholders but also other stakeholders. Grais and Pellegrini (2006), state that more accountability and

greater transparency as components of good corporate governance practice will positively affect the growth of firms' improving their stability and trustworthiness.

The role of corporate governance is vital in helping firms achieve their specific objectives and goals. For financial institutions, the distinct function of corporate governance is mainly concentrated on the set of legal rules, determination of firms' policies, the board of directors, the managers and their behaviours towards shareholders, depositors and other stakeholders. The complication of financial firms with a larger group of stakeholders affects the corporate governance framework. These factors also lead to the distinctive guidelines and codes to promote best practice of corporate governance in financial institutions.

2.3 Theories related to Corporate Governance

The following sections discuss theories and perspectives relevant to this study, which focuses on the relationship between corporate governance and the performance of Malaysian financial institutions' and explain corporate governance mechanisms in terms of each theory. The following chapter presents a more comprehensive review of theoretical and empirical literature in order to explain how every corporate governance mechanisms might affect the firm's performance.

2.3.1 Agency Theory

Several corporate governance studies are originated from or guided by agency theory. In the opinion of, Berle and Means (1932); Eisenhardt (1989) and Donaldson et al. (1991) agency theory in case of corporate governance is obligatory with the intention of ensuring that the principal-agent risks and problems are alleviated. An agent is claimed to be such a person who accomplishes all the required responsibilities to perform certain work in support of other individual (the principal). Constitutionally, agency theory observes the relationships that exist between the individuals (managers) and the way they are contracted to work for the interests of the owners (principals) and also about the conflict of interests arises. Daily et. al (2003) remonstrated that humans are not eager to surrender their personal interests for the superlative interests of others. Therefore, each individual in an administration is encouraged to raise his/her own interests which are suggested by agency theory. According to, Clarke, (2004), the severance between management as the control and shareholders as owners is a common exercise in case of corporate structure, as a response to the nature of the modern corporations, which have a scattered ownership structure.

Corporate governance is an apparatus by which the board of directors would supervise and reduce the disagreement of interest and the managers-owners' problems as in the opinion of Berle and Means (1932). Jensen and Meckling (1976) referred the firm as a connection of contracts between individual factors in the disclosure of the agency theory. The firm is a split legal entity and not an individual, where divergences of interests and objectives of individuals live. In order to bring such conflicting issues into equilibrium, they are always supervised by contractual arrangements. On the authority of Jensen & Meckling, (1976), in respect to contractual arrangements and relationships are appeared into between and among many

businesses recounted parties that comprises shareholders, managers, customers, suppliers, creditors and employers. However, these corresponding contracts are eloquent in order to retain and defend the right of each individual engaged and to maximize the value of their organizations. In addition to this, in case of achieving this minimising agency costs and executing accounting methods to most proficiently imitate their own performances are two methods as obliged by (Deegan, 2006).

Agency theory proposes a set of assumptions for governing corporations that normally encompasses of a great number of shareholders. Moreover, in order to organize and manage their investments for the reason of producing future profit and consequently enhance their wealth, these shareholders allot to managers responsibility. Although, these managers may not always have possession of shares in the corporation, but may possess an elevated level of understanding and occurrences in managing the corporation in the best possible manner as declared by (Aintablian and Boustany, 2008). In spite to minimise such conflict of interests between managers and shareholders is to align the interests of both the principal and the agent in one direction suggested by the resolution of the theory. As a matter of fact, corporate governance is fundamentally about concern of misuse of shareholders' resources by their managers (Clarke, 2004). Thus, Ang et al. (2000) stated that, as a result of misalignment of interest between the owner and the agent, agency costs occur.

Correspondingly, Jensen and Meckling (1976) claimed that, agency cost comprises three components: monitoring, bonding and residual loss. Monitoring cost is the cost acquired by the principal to diminish the uncertain behaviour of the agent. In the same way, bonding cost is referred as the cost incurred to certify that managers' decisions are taken for the interest and benefits of the principals. Lastly, the cost incurred when both the monitoring and bonding

costs have failed to control the assumed opposing and divergent behaviour of managers is stated as residual loss. In support of these effects on the agency cost and internal inefficiencies, agency theory recommends that corporate governance machinery are the tool to make sure that their investments are protected and their values are increased by monitoring and controlling manners and decisions of managers (Jensen & Meckling, 1976). On the authority of, by using agency theory Turnbull (1997) terminated that, shareholder value cannot be enlarged; all because of managers and executives get pleasure from the discretion which eventually permits them to side track shareholder values for their own personal benefits.

On the whole, agency theory advocates facts about human behaviour applied to the behaviour of managers and executives and guides not only investors, similarly incorporate regulatory bodies through frameworks developed by its assumptions. Although, by using the assumptions of agency theory, analysis in addition to the structure of corporate management can be sensibly shaped and articulated for the profit of shareholders, corporate entities and the business environment primarily by allocating investment security.

2.3.2 Stewardship Theory

Contrary to agency theory, which focuses on managerial opportunistic individualism, stewardship theory suggests that executive managers are intrinsically trustworthy individuals. Stewardship theory prioritizes on psychological and sociological methods of misunderstanding, more willingly than the economic (pecuniary) tools of agency theory. In accordance with Davis et al. (1997) the former holds that organisational members encompass certain form of positive collective personality that eventually provokes trustworthy

behaviour. Muth and Donaldson (1998) concur in that financial gain is not essentially the sole driver of managerial behaviour and additionally managers require some discretion to manage the business for shareholders. Subsequently, separate ownership is not observed as a weakness in stewardship theory as cooperative behaviours are meant to be the intrinsic behaviour of managers stated by Donaldson and Davis (1991); Davis et al. (1997) and they are the subject matter to an array of motives as well as to financial gain proposed by (Muth and Donaldson, 1998).

Stewardship theory conceives that apprehension for their own reputations and career progression restrains agents from acting in opposition to the interests of shareholders, therefore agency costs must be inherently minimised (Donaldson and Davis, 1994). On the authority of Clarke (2004), the involvement to firm performance of stewards associates with the context regarding socio-cultural and psychological factors. Managers are considered to execute better with greater empowerment and job approval which is a psychological aspect. Socially, managers (along with most personnel in a successful organisation) normally self-identify as organisational representatives and since then they take under account the power accorded them by principals to be a tool for facilitating the organisation and other member of staffs to accomplish the organisational purposes. In case of situational perspective, it is predicted that managers work optimally in an environment that is participation-oriented (i.e. areas in which completion of tasks, control and thoughts are merged in a single procedure). Nevertheless, this will obviously have implications on the long-term relationship and loyalty that managers have towards the firm if the organisational culture has a collective orientation (Clarke, 2004).

Stewardship theory holds that an insider-dominated board is more effectual because it possesses more in-depth knowledge of organisational operations like, access to data and technical expertise (Muth and Donaldson, 1998). In addition to this, CEO-Chairman duality will make leadership and management more constant, particularly on the subject of decision making and strategy (e.g. investment), which is also supposed to contribute to greater success (Donaldson and Davis, 1991). Because the inside directors have more widespread and deep knowledge of daily operations within firms, their decisions are better enlightened. As said by stewardship theory, they are hence preferable to NEDs, because of their more exact knowledge of firm performance. However, with fewer inside directors, boards have decreased insight into the company's situation and advancement, providing them dependent on information embellished by the management along with little or no contextual knowledge in order to make any decisions self-regulating of the recommendations of managers, NEDs undergo from this similar lack of knowledge as the board in general. On the whole, reduced aptitude to oversee the managers and the making of less informed decisions by boards incorporating outsiders signifies that such boards are improbable in order to progress firm performance to the same extent as boards with a huge number of insider directors as believed by stewardship theory.

2.4 Corporate Governance in the Financial Institutions

Good corporate governance practice is crucial for financial institutions. The misconduct and corporate failure of several financial institutions have occurred, because of weak corporate governance framework (Schachler et al., 2007). There are different significant issues of corporate governance that affect the governance structure in the financial institutions such as heavily regulated and impeded common governance mechanisms, government ownership and

the ambiguousness of financial institutions that adjust the corporate governance equation (Caprio and Levine, 2002).

The government or regulatory authority normally imposes certain regulatory requirements on banks, such as rules on deposit insurance, limitation on certain activities and restriction on shareholders. In addition to this, there are some important governance variables in the financial sectors, mainly in terms of board composition, size, ownership, board activity and CEO compensation. These exceptional characteristics imply the need for effective corporate governance measures for the financial firms. This is also supported by Macey and O'Hara (2003) in their study on corporate governance as they focused on the need for additional measures of corporate governance for financial institutions.

In order to have safe and sound governance practices, the Basel committee on Banking Supervision (BCBS) has taken the initiative to provide guidelines on improving corporate governance system for firms because of the unique characteristics of corporate governance in financial institutions. Unlike the general principles of corporate governance by OECD, which are applicable to all types of corporate entity, the corporate governance standards provided by BCBS are more specific and exclusive to the financial institutions.

The above studies and research on corporate governance suggest that multiple approaches to the model of corporate governance are crucial within the context of financial institutions. The diversity in the financial institutions compared to other corporate entities comes mainly from the presence of different stakeholders, such as shareholders, regulators, depositors and investors (Yamak and Suer, 2005). This circumstance states that board of directors and

managers are assumed to have duty towards all stakeholders and it needs a unique corporate governance system as a mechanism to control the firms. Yamak and Suer (2005) identified the major stakeholders in financial institutions and classified them into the owners, the regulators, the depositors, the borrowers, and the managers. The owners and the shareholders expect to maximise the firms' profit, the regulators shows interest in the compliance to laws and regulations by all the stakeholders; the depositors assume return on their deposits; the borrowers are concerned with fair and non-discriminatory treat by the organisations and; the managers assume that they obtain financial and non-financial compensations. Identifying the rights and interests of all the stakeholders', the corporate governance model in the context of financial institutions seem to be more complex than in any other types of organisations and shows for the practice of a specific model to practice.

2.5 Good Corporate Governance Practice and Firm Performance

Corporate governance has become a considerable issue worldwide and an essential ingredient for the stability of firms and long-term economy. It is important for the growth of the country's economy. Therefore different markets and countries have used the basic and common OECD principles and guidelines to bring about the good codes of corporate governance practice. Good governance practice stands for 'little expropriation of corporate resources by controlling shareholders or by managers, which contributes to better allocation of corporate resources and firm performance.

Renders et al. (2010) found a positive correlation between good corporate governance and firm's financial performance. On the other hand, a study by Gupta et al. (2013) was not able to confirm a positive correlation. Based on the findings of previous empirical studies on the relationship between corporate governance and firm performance, it can be said that the empirical studies along with the theory does not define exactly what good corporate governance is. Instead, prior studies have explored several characteristics of good corporate governance such as board size, independence of the board, frequency of meeting, board compensation and other variables. Therefore, for instance Castaner and Kavadis (2013) explored clearly 'good' corporate governance using a collection of governance variables rather than defining the term. The same goes for different codes of corporate governance in different countries. OECD (2015) mentioned that each country has its own model of corporate governance, which consists of country-specific cultures, history and circumstances.

2.6 Corporate Governance and Firm Performance in Malaysia

In accordance with Haniffa and Hudaib, (2006), the importance of possessing good corporate governance had not received much concentration in Malaysia. Particular corporate disintegrates occurred, for instance Berhad, Renong Berhad, and KFC Holding Berhad, due to the deficient of effective corporate governance mechanisms before the Asian financial crisis in 1997 and 1998. As can be seen, this designates that in Malaysia poor corporate governance donated to the financial crisis. In the same manner, the crisis in Malaysia has provided adjoined momentum in order to corporate governance reforms. However, in 2000, the Malaysian government has instituted the Malaysian Code of Corporate Governance (MCCG) as foremost initiative, which identifies a framework for best practices in case of corporate governance. Moreover, the Malaysian corporate has experienced advancement on a

episodic basis. As has been noted, the Malaysian government casted corporate governance codes as Malaysian Code of Corporate Governance (MCCG, 2000, 2007 and 2012). As a result, intensive efforts with the intention of reforming corporate practices in sponsoring corporate governance in Malaysia has been made by the high-level Malaysian finance committee.

In compliance with Hamza, (2013), in Malaysia the Sharia governance framework is based on the centralised model as contrasted to the decentralized being practiced in the GCC countries. Therefore, on the basis that the Central Bank itself has its own Shariah supervisory board called the Shariah Advisory Board and all Islamic financial institutions are required to form their own Shariah committee that must comply with the rules set by the Shariah Advisory Board of the Central Bank, the centralised model is formed. In obedience to the comparative studies conducted by Mollah and Zaman (2015) between conventional and Islamic banks on the correlation between Shariah administration, corporate governance and performance, the final results indicate that supervision boards are positively impact on Islamic banks performance because of their roles in case of shielding the shareholder concern and acquiescence towards Shariah principles. Additionally, Maurya, et al. (2015) designates that there exists a very well-built and positive connection among the size of board of directors and numeral of associates of the Shariah Committee towards banks performance.

On the contrary, Garas (2012) argues that the number of Shariah Committee members insignificantly concludes their power over the financing and investing activities of Islamic banks. On the contrary, it has been disagreed that elevated number of Shariah committee constituents escorts to disputes that resulting in inadequacy in decision making process. On

the authority of Wan Abdullah, et al. (2013) found that, there appears insignificant association among the size of Shariah board and the coverage of Shariah disclosures in the annual reports of Islamic banks in Malaysia.

2.7 Association between Corporate Governance Variables and Firm Performance

This section will describe the association between the governance variables and firm performance which will help to build up the hypotheses for this study.

2.7.1 Board Size and Firm Performance

Board size refers to the total number of directors on the board of directors that are on the firm's board. There are several evidences of empirical studies conducted on the influence of board size on firm performance (Dalziel and Hillman, 2003 and Fuzi, et al. 2016). There is argument on the effect of the size of the board on firm performance that it may not just vary by firm level characteristics but also by country-specific factors, such as; legal practices, institutions and governance mechanisms (Karamanou and Vafeas, 2005). Ntim et al. (2015) suggest in the empirical studies that country-specific factors, such as governance mechanisms, legal framework, culture, religious and ownership structure affect the composition of the board and, as a result, they affect board monitoring function and firm performance.

Latif et al. (2013) monitored the effect of corporate governance mechanisms on firm performance and they also figure out a noteworthy positive affiliation among board size and

firm performance. Therefore, their final outputs support Zahra and Pearce's (1989) termination about the authority of board size on firm performance. As a consequence, previous studies those were conducted by John and Senbet (1998), Dalton et al. (1999), Haniffa and Hudaib (2006), Yawson (2006), Lehn et al. (2009) established that large boards endow with wider multiplicity of backgrounds, diversity in communications skills, experiences and business contacts outside the company.

Similarly, Dalton et al. (1998) claimed that larger boards consent to the directors to swap over more highly skilled counsels and represents additional scope for the opportunity of correspondence with different exterior linkages. Moreover, by performing their strategic function more effectively, which is essential during periods of financial turbulence to reduce agency problems and these problems are controlled by the larger boards (Mintzberg, 1983). Surprisingly, the deficiency of diversity in smaller boards arises uncertainty concerning strategic development under such circumstances as stated by (Pearce and Zahra, 1992) and (Goodsteing et al. in 1994). On the whole, this eventually enlarges the agency problem and undermines performance in firms with smaller boards.

On the contrary, Chaghadari (2011) justified the significance of one of the corporate governance means which is, board size of companies listed on Bursa Malaysia and functional linear multiple regression as the fundamental statistical test. Moreover, the study did not discover a noteworthy association among board size and firm performance in the sample of selected listed companies in Malaysia. On the other hand, further study accomplished by Kajola (2008) was absolutely about the alliance between the corporate governance mechanisms and firm performance of a sample of 20 Nigerian listed firms did not locate a

considerable connection involving the board size and firm performance of the listed companies in the Nigerian Stock Exchange.

Consequently, the Malaysian Code and the KLSE Listing Requirement were soundless about the number of directors that should appear on board. However, it was suggested that the board size should not be too big nor too small but satisfactory enough so that to allow for active and effectual involvement and they should be able to execute their duties in point of fact. Additionally, few companies may not pursue these instructions and commendations. Since not all the companies have the same size and the same style of work. Thus, the size might differ from company to another company.

Nonetheless, in accordance to Sharma (1985) small board size is easily influenced by senior managers. On the whole, it can be argued that when board size is large, the capability of the board to organize managers become effective in controlling agency problem and improving firm performance. In the conclusion, agency theory predict that the size of the board illustrate the level of control by the management team. Therefore, this study conjectures that board size is related to firm performance.

2.7.2 Board Committees and Firm Performance

Several past evidences have considered the number of board committees as a vital measurement for firm performance. Board of directors have fiduciary duties of acting on behalf of the shareholders (Fama and Jensen, 1983). In practice, the board delegates most of the duties to board committees (Adams, 2003; Guo and Masulis, 2015). Some of these committees are made ad-hoc for a particular task, whereas standing committees are delegated with specific, narrowly defined tasks. Important board decisions are initiated in these committees and evidence shows that the delegation of duties to committees facilitates effective corporate governance (Billmoria and Piderit, 1994; Adams, 2003). The references of these committees are placed before the full board for discussion (Klein, 1998). According to S&P 500 (Standard & Poor's 500) sample, all firms have minimum one standing committee, with the average firms having three committees. Most common committees among these are audit committee, nomination committee and remuneration committee.

Concurring with the agency model, the Cadbury Report (1992) argued that board committees are an additional control mechanism to encourage increased accountability and optimum financial management of firms, with increased protection of shareholder interests (Cadbury, 1992). Harrison (1987) argues that shareholder protection and generally responsible behaviour can be induced in corporate boards due to the successful application of board committees. The specialist functions of board committees thus promote the credibility, legitimacy and accountability of corporate governance. The practical implications of board committees are reflected in the fact that a significant proliferation in their use has occurred since the early 1980s (Harrison, 1987), and most corporate governance codes advocate such

committees (Cadbury Report, 1992), mainly related to functions concerning nomination, remuneration and auditing committees.

Shivdasani and Yarmack (1999) found that if the CEO is on the nomination committee, then firms appoint few independent directors. Guo and Masulis (2015) states that firms with full of independent nomination committees have higher sensitivity of forced CEO turnover, and nomination committee independence is significant even when firms have independent boards. In contrast, Anderson and Bizjak (2003) find that independence of compensation committee and the presence of CEO does not affect executive compensation. Committee independence also affects the timing of earnings announcement (Michaely, et al. 2014).

2.7.3 Board Meetings and Firm Performance

According to the requirement of Malaysian Code on corporate governance, companies are encouraged to have regular board meetings for discharging duties and responsibilities. Also, it is mandatory for the board to disclose the number of board meetings held in a year and details of the attendance of each individual director in respect to meetings held. Frequency of board meetings is considered to be an important way of improving the effectiveness of the board (Conger and Lawler, 2009; Adam and Ferreira, 2009). It is argued that board meetings and attendance of the meetings are considered to be important channels through which directors obtain firm specific information and able to fulfil their monitoring role. A study conducted by Francis et al. (2012) indicated that firms with poor board attendance at meetings perform significantly worse than boards which has good attendance during financial crisis. In addition, Ntim and Osei (2011) conducted a study in South Africa which also

suggested similar findings between the frequency of board meetings and corporate performance where boards that meet more frequently tend to generate higher financial performance.

On the other hand, there are researchers who consider board meetings not necessarily useful due to the limited time non-executives spend with the company and consider such time could be better utilised for a more meaningful exchange of ideas with the management (Vafeas, 1999). The effectiveness of the corporate board is highly based on the frequency of their meetings (Lipton & Lorsch, 1992). It is believed that the frequency of board meetings affect corporate performance (Jensen, 1993; Vafeas, 1999). Ntim and Osei (2011) stated that a statistically significant and positive association exists between the frequency of corporation board meetings and corporate performance, implying that South African board that meet more frequently tend to generate higher financial performance. The study provided an empirical support for agency theory, which suggests that corporate board that meet more frequently have increased capacity to effectively advice, monitor and discipline management, and thereby improving corporate financial performance.

2.7.4 Proportion of Non-Executive Directors and Firm Performance

The board comprises of executives and non-executives who are either independent or non-independent directors. The non-executive directors (NEDs) need to play a role in monitoring the actions of the CEO and executive directors to ensure that the shareholders' interests are well cared for and to add to the diversity of skills and expertise of the directors (Weir and Laing, 2001) and (Abdullah, 2004). The Malaysian Code on Corporate Governance (2000)

and the revised code (2007) recommend that it is the best practice to have a balance membership board of directors where independent NEDs should make up at least one third of the board membership. This is to ensure the effectiveness of the independent directors in maintaining good decision making for the company. In Pakistan, Awan et al. (2012) discovered a positive relationship between NEDs and firm performance measured using return on asset (ROA) and return on equity (ROE). Another study that was conducted among Belgian companies found a significant relationship between the number of outside directors and ROE which supports the notion that outsiders are able to perform a monitoring function as a result of their independence and the interest of the shareholders are well protected (Dehane et al, 2001).

Despite the advantages of having more NEDs on the board, prior studies have shown contrary result from the analyses of the relationship between the NEDs and firm performance. According to Weir & Liang (2001) non-executive directors are only employed on a part-time basis and are therefore likely to have other work commitments, they may lack the expertise necessary for understanding highly technical business issues and may have insufficient information when required to make key decisions. A study conducted by Abdullah (2004) in Malaysia used data from the (KLSE) Main Board for the period between 1994 and 1996 found that there is no significant difference in performance between firms with independent boards and firm with non-independent boards. Similar findings are reported by Rahman and Mohamed Ali (2006) non-executive directors had no influence on firm performance. This could be due to in many developing countries including Malaysia the selection of the independent directors is not based on their expertise and experience but more for political reasons to legitimate business activities and contracts (Haniffa & Hudaib, 2006).

In contrast, a study conducted by Salleh et al. (2005) found that a higher percentage of non-executives has created better auditing systems and improved financial reporting timeliness (Abdullah, 2006). Abidin et al. (2009) found evidence that a higher proportion of independent non-executive directors on the board have a positive impact on firm performance based on value added intellectual coefficient measurement. This study addresses and investigates the conflicting issue of whether a high proportion of outsider directors have an impact on the firm performance of an organisation.

2.7.5 Women Directors and Firm Performance

A growing number of studies in recent years have explored the influence of board diversity on the firm outcomes (Terjensen et al. 2009) and particularly the gender diversity is measured by the presence of women directors on the board (Hillman, 2015; Post and Byron, 2015). Existing academic research not only indicates that less women on the boards relative to their presence in the population but also shows that gender diversity on the board able to increase benefits to the organisational outcomes (Burgess and Tharenou, 2002; Simpson et al., 2010; Terjensen, 2015).

Firstly, a gender diverse boardroom is argued to be associated with better quality decisions than the male only boardroom (Milliken and Martins, 1996). Male and female directors often differ in their backgrounds, core values, perspectives and risk attitudes (Simpson et al., 2010; Adams and Funk, 2012). As a result, gender diversity on board may bring down benefits to the firms' through their experiences, skills, knowledge, information and networks (Hillman et al., 2007). Previous studies indicate that in comparable to male directors, most women

directors are likely to have managerial and public relation skills rather than marketing and operating functions (Zelechowski and Bilimoria, 2004). They are more likely to have non-business backgrounds and hold more advanced degrees (Hillman et al. 2002), which assist the firms to achieve competitive advantage and handle more effectively with their product diversity and labour markets (Bilimoria and Wheeler, 2004).

In accordance with the 'value in diversity' previous studies also suggest that women directors have diverse point of view which promotes the boardroom discussions (Letendre, 2004) and transparency (Upadhyay and Zeng, 2014). Many studies have empirically examined the relation between women directors on the board and firm performance (Ahern and Dittman, 2012; Matsa and Miller, 2013; Goergen and Renneboog, 2014). Recent studies on microfinance institutions noted that more number of women on the board is able to lower the operating costs (Chakrabarty and Bass, 2014) and influence the firm performance (Storm et al., 2014).

On the contrary, several papers have found no relationship or negative relationship between the percentage of women directors on board and firm performance. For instance, Smith et al. (2006) found a negative relationship between gender diversity and gross profit to sales.

2.7.6 Firm Size and Firm Performance

Shaheen and Malik (2012) referred to firm size as the measure and array of production capability and potential a firm possesses or the diversity and quantity of services that a firm concurrently make available to its customers. Firm size plays an important and effective role in explaining the kind of relationship it has within and outside environment it is operating.

Babalola (2013) argued that large firms outperform small firms, so the larger a firm is, the more it influences its stakeholders. The model of economies of scale theoretically supports the positive correlation between firm size and profitability and this justification was noticeable in studies conducted by Babalola (2013), Kumar and Kaur (2016) and Kartikasari and Merianti (2016). However, the outcomes of these studies have been controversial and inconsistent, whereas, some academics and scholars found positive relationship while others found negative relationship.

2.8 Summary

This chapter critically analyses the assumptions and arguments of corporate governance theories and its application to modern companies. This chapter also discussed the mechanisms of governance and their effect on financial performance. In addition, it presents the relationship between governance variables and firm performance. The review of literature will help to build up the hypotheses which determine the relationship between corporate governance and firm performance.

Chapter 3: Literature Review 2: Impact of Shariah Supervisory Board (SSB) on Malaysian Financial Institutions' Performance

3.0 Introduction

This chapter discusses the SSB, their role in financial institutions and how it influences the firm performance. The SSB is one of the most important governance mechanisms of an IFI to ensure compliance with Shariah which is a distinctive characteristic of an IFI as compared to its conventional counterpart. Acknowledging this important characteristic, the Accounting and Auditing Organization for Islamic Financial Institution (AAOIFI) has issued a set of standards on SSB, Shariah review and internal Shariah review; all collectively known as governance Standards (AAOIFI, 1999). Besides these standards, Malaysia and several other countries have also passed laws to govern the formation and function of SSB. This chapter reviews relevant literature that examines SSB practices and the extent of their impact particularly on the Malaysian financial institutions.

3.1 Shariah Supervisory Board (SSB)

Shariah board (SB) is considered as an essential key participant in the governance of Islamic companies found in Islamic organizations. Therefore, it is a part of the governance framework of Islamic business (El-Ghayad, 2008). Several researchers have characterized the board. Garas and Pierce (2010) provide that “the SB is a group of Islamic scholars, appointed by the shareholders and similar to the board.” Thus, Accounting and Auditing Organization for Islamic Financial Institutions (AAOIFI) governance standards put SB on par with the

board of directors. Similarly, the Islamic Financial Services Board-10 (IFSB-10) defines the Shariah Supervisory Board (SSB) as a body made of a panel of Shariah scholars that provide Shariah expertise and act as an advisor to the institutions. The member of SSB is responsible for the follow-up the tasks and the validity of the implemented transactions in the IB and to find legitimate solutions to the irregularities. The SSBs also responsible for following up, examining, analysing activities, business, behaviours, and operations that carried out by the several Islamic Financial Institutions (IFIs), to ensure that they are in accordance with the rules and principles of Shariah. Choudhury and Hoque (2006) state that SSB or a Shariah advisor guide Islamic financial institutions as a legitimate control body.

According to the SSB Functions, the purpose of the SSB is to ensure that the financial institutions operate in conformity with Shariah and are usually made up of a number of jurists who provide clarification in regards to any questions that the financial institutions may have (Rammal, 2006). The financial institutions appoint the SSBs to act as an internal control body in the firms, therefore increase the credibility in the eyes of customers (Algaoud and Lewis, 1997).

Malaysia is one of the leading countries and backbone of the Islamic financial industry in the world (IFN, 2015). It involves the Shariah Advisory Council (SAC) as a Council for Fatwa, which mainly follows the Central Bank of Malaysia. This Council was established in 1997 to provide the highest Shariah authority for Islamic finance in Malaysia. SAC has the authority of certainty of Islamic law for the purposes of Takaful business, financial business, Islamic financial business, Islamic banking business or any other business that is based on Shariah principles and regulated by Bank Negara Malaysia (BNM, 2016).

3.2 Role of SSB in Financial Institutions

Role of Shariah board depends on the degree, nature and extent of Shariah compliance and it also varies from one to another board. Inspired by its shareholder value orientation and its foundational dimension, the Shariah board has fiduciary duties to all its stakeholders. Besar et al. (2009) states that the role of SSB is to emphasize on the matter relating to Shariah compliance and generally do not participate directly in the risk management process as evidenced from the annual reports of firms that they do not appear in the risk management committee. The opinion of the Shariah supervisory board members on Shariah related matters are placed to the board of directors to take the final decision. Thus, it is important to know whom SSB is liable to and how far its existence is truly relevant.

A study conducted by Hasan (2011) indicates that SSB is accountable to the board of directors in many respects, since their appointment, dismissal and remuneration depends on the approval of the board of directors. However, SSB is one of the stakeholders of the financial institution, so the nature of their decision making may influence the approval of a product over another; their decisions are debated on the level of board of directors as well as internal auditing level. Therefore, their decision matters to the increase or decrease of the volume of business. The main role of the SSB in the financial institutions is summarized in the participation to formulate the instructions, regulations, forms of contracts, correction and development. They are also responsible for supervising the activities of the firms to ensure the conformity of its works to Islamic legal precepts and principles (Gulzar, 2006).

3.3 Shariah Governance Process

Literature documents several characteristic of SSB such as appointing the board members, composition of the board, qualification of SSB members, expertise may have an impact on the efficiency of SSB (Farook et al., 2011; Rahman and Bukair, 2013). This section will describe the SSB governance process which might influence firm performance.

3.3.1 Appointment

In existing practice, the Board of directors or the shareholders appoint the members of the Shariah board in the annual general meeting (AGM). The document of International Association of Islamic banks (IAIB) mentions that, in order to ensure independence and freedom, a Shariah board members must not be a staff from the bank is not subject to the authority (Rammal, 2006). Furthermore, the AAOIFI governance standard states that the shareholders have the right to appoint Shariah board members during the annual general meeting. The Shariah board members are allowed to place their decisions on the board meetings and discuss religious issues (Nathan and Ribiere, 2007).

3.3.2 Educational Qualification

A well-educated member in the board positively deals with the new challenges and improves the quality of the board (Kakabadse et al., 2010). Therefore, there is a positive relation between the qualified Shariah Board members and firm performance (Cheng et al., 2010). The educational background always has been a major factor in the discloser practice (Farook

et al., 2011). In respect of SSB, the more qualified Shariah board members the more profit for the business (Musibah and Alfattani, 2014). It is expected to be better versed in finance and banking sector if the board member have a doctorate degree (Farook et al., 2011; Rahman and Bukair, 2013; Nomran et al., 2018). Nonetheless, there are Shariah scholars even without any academic degree or qualification or in Shariah related studies (Bakar, 2016).

3.3.3 Board Composition

A Shariah board usually comprises of Shariah scholars who are experts in *usul al fiqh* and *fiqh al muamalat*. The composition of the board members varies from one institution to another. The Shariah board normally consist of regional scholars, whereas in individual Islamic financial institutions are comprised of local scholars. The IFI appoint three to six members on the Shariah board. The AAOIFI Shariah board is comprised of not more than twenty people and they are among the Shariah scholars. Malaysia is one of the countries that follow the AAOIFI standard requirement for standard composition of Shariah board.

3.3.4 Expertise

Shariah board members are scholars in Islamic commercial jurisprudence with expertise in the field of Islamic financial institutions (IFI) comparing to the board of directors (AAOIFI, 2005; Al-Qattan and Abdul Sattar, 2007) which make them able to fulfil their accountabilities in supervising the financial reporting. Similarly, the study conducted by El-Chaarani (2017) shows that the existence of Shariah supervisory board members with certain types of

expertise affects the level of disclosure because of their awareness of the importance of transparent reporting.

The Shariah scholars' shortage of knowledge causes governance practices to face challenges. Some of them have the lacking of knowledge on Shariah based law and misinterpret the rules (Chowdhury and Sarker, 2015).

3.4 Shariah Supervisory Board (SSB) and Firm Performance

According to Choudhury and Hoque (2006) Islamic corporate governance is a faith based theoretical framework that is regarded as a theory that relates to the process of decision-making using the principles of the Islamic socio-scientific epistemology of Tawheed, oneness of God. The influence of the Islamic view of corporate governance is significant, particularly when related to transaction cost minimization in decision-making environments and achievement of the objectives of the corporation within the framework of Sharia law and Islamic rules and principles (Choudhury & Hoque 2006).

The main distinguishing attribute of Islamic corporate governance is the mandatory presence of a Sharia Supervisory Board (SSB) as all business transactions have to be Sharia compliant (Alman 2012). Bukhari et al. (2013) study found that board of directors and Shariah Supervisory Board are the most significant dimensions that influence corporate governance. Alman (2012) observed that the increasing size of SSB influence the loan portfolio risk-taking of Islamic financial institutions. Quttainah et al. (2013) suggest that small SSB size may reduce the agency costs and may increase the coordination between the board members.

Similarly, Yarmack (1996) states that smaller size of the BOD facilitates the communication among the board members thus make the decision making process more effective.

As for the Shariah supervisory board, small size board is more manageable and easier to monitor comparing to the large size SSB. Another argument supported large size SSB as it may comprise of various skilled and experienced scholars and schools of *fiqh* which may lead to a better understanding of the products and thus eventually better performance (Hamza, 2016).

3.5 Prior Studies on Shariah-Based Corporate Governance

The modern Islamic finance industry has been growing rapidly and strong practice of Shariah laws are needed to support this growth. To illustrate, Abdullah et al. (2012) presented the correlation between different governance structures of Islamic and conventional banks. Chapra and Ahmed (2002) showed that when any infringement of Shariah laws occurs, most of the depositors in IFIs would withdraw their money. In addition, they also found that the growth of Islamic finance industry is emerging swiftly in South East Asia and Middle Eastern countries.

But on the contrary, high capital ownership and family business are conspicuous features of this market. Surprisingly, the consequence of these markets is the security of minority shareholders and investment account holders (IAHs) for IFIs are very fragile (Darmadi, 2013). Garas (2012) examined the incompatibility between Shariah Committee and board of directors and other third parties and found that the major reason behind the confliction in the Shariah Committee is the executive position which is held by Shariah Committee members.

Grassa and Matoussi (2014) investigated the governance structure of Islamic banks in Gulf Cooperation Council and Southeast Asian countries including the governance practices and found the limitations of the current governance framework for Islamic banks which require further development and enhancement.

3.6 Summary

This chapter aims to provide SSB characteristics and whether they play an important role in financial institutions. It has also critically analysed the literature from the prior studies based on Shariah based corporate governance and the monitoring system.

Chapter 4: Research Methodology

4.0 Introduction

This study investigates the performance of Malaysian financial institutions and understands whether SSB as a governance mechanism influence the firm performance. This chapter presents the research philosophy and explains the methodology that was applied in undertaking the research and it also justifies the use of quantitative research methods in analysing the variables and testing the hypotheses.

This chapter is structured as follows. Section 4.1 covers the research paradigm, which is primarily a positivist approach. Section 4.2 considers and evaluates the research methodology to achieve the objectives of the study; it thus focuses on the quantitative methods mainly through the use of regression and secondary data gathered from different sources. Section 4.3 includes the proposed hypotheses. Section 4.4 introduces the dependent and independent variables, control variables as well as the performance measure variables. Section 4.5 discusses the sample selection and justification of the sampling period. The final section presents the testing procedure which is the regression analysis, and the use of STATA in running the analysis.

4.1 Research Paradigm and Philosophy

Burrell and Morgan (1979) argue that researchers must select the proper paradigm for their study. Henn et al. (2006) states, paradigms can generally be classified either as positivist or interpretive paradigms. This study takes the positivist paradigm in which the hypotheses are developed based on the idea of the impact of the corporate governance on the Malaysian firm performance that can be investigated and empirically examined using the researcher's tools of analysis and the theoretical conjectures. The study uses deductive reasoning and quantitative techniques because the positivist approach seeks causes or facts and effects of social phenomena (Hussey and Hussey, 1997). Bryman and Bell (2007) indicate that the deductive approach is related to quantitative research that follows objectivism, ontological realism and epistemological positivism.

Saunders et al. (2009) affirmed that deduction is linked to positivism, and fulfills the need to describe the casual association between or among variables and the need to generalize a conclusion. Accordingly, the nature of this study implies implementing deductive rather than inductive approach for the following reasons (Saunders et al., 2009):

- It is used to testing hypotheses rather than to building new theory.
- It tends to be informed by scientific principles rather than gaining further understanding of human-constructed meanings related to events.
- It identifies casual relationships amongst variables rather than clarifying the research context.

- It uses quantitative data.
- It is a more structured approach than inductive approach.

In summary, the research paradigm of this study is informed by the fact that the study does not seek to produce a new theory but to test existing hypotheses based on analysis of quantitative data, thus the deductive approach is more appropriate for this research. This in turn brings to the discussion of philosophical stance on whether the issue of SSB and financial institutions' performance can be appropriately ascertained and understood. While this study attempts to provide some evidence of the relationship, by no means it suggests that the presented evidence is absolute. Attempts are made in ensuring the methodology is rigorous and this is discussed in the next section on research strategy, design and approach.

4.2 Research Strategy, Design and Approach

Research strategy helps researcher to investigate the research issues. According to Saunders et al. (2009), research strategy is a general plan, which helps to answer the research questions in a systematic way and also helpful to use specific data collection methods to support the arguments.

This study uses a total of 50 financial institutions listed on the main board of the Bursa Malaysia and excluded 7 companies which do not have the required information. Secondary data used for the period of 2012 to 2016. The data collection method follows the technique adopted by previous studies (La Porta et al., 1998). Consistent with prior literature, the

dependent variable, which is the performance, is measured by return on assets (ROA) and Tobin's Q (Musibah and Alfattani, 2014; Grassa and Matoussi, 2014; Mollah and Zaman, 2015). Firm performance assessed by ROA is the most common ratio to measure the performance. All the independent variables selected in this study were collected from the firms' annual report giving information on corporate governance mechanisms such as board size, non-executive directors, board committees, board meeting and women directors. In this study, independent variable like proportion of women directors on SSB were selected to examine its impact on firm performance.

In accounting studies, quantitative approaches have become more popular as a result of the increasing availability of electronic database sources such as DataStream, Bloomberg and Compustat and online annual reports which provide financial information and data. Researchers of quantitative studies are engaged with the prediction, manipulation, and testing of empirical variables, emphasising research design, procedure, and statistical measures of validity (Nachmias and Nachmias, 1996).

In short, the current study will use one type of data collection method, which is quantitative data (DataStream and annual reports). An OLS regression model is the primary technique used to determine the variables' influence on the relationship between corporate governance and firm performance.

4.3 Research Hypotheses

This section discusses the following six hypotheses that are tested in this study.

4.3.1 Board Size

Several studies found that larger boards put more effort to compromise and negotiate among members, thus their decisions are more shaped and less likely to satisfy different opinions than those of smaller groups (Kogan and Wallach, 1965). Sah and Stiglitz (1991) compared the result of group decision-making and noticed that larger groups had a diversification of opinion effect which lowered the possibility of accepting bad projects. On the contrary, Lipton and Lorsch (1992) found evidence that smaller groups are more often result in better firm performance. Lipton and Lorsch (1992) also argued that larger board may have less efficiency because of difficulties in solving agency problems among members of the board.

Cheng (2008) examined the effect of different board sizes on variability of corporate performance and found the empirical assumption that larger board make less extreme decision and thus have less variable performance. On the other hand, smaller boards are more likely to have extreme short wins and losses. Thus it is possible to assume that larger boards are much better at achieving a higher level of firms' performance.

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

4.3.2 Non-executive Director

According to the stewardship theory, NEDs are less capable of monitoring the managers than inside directors because of their lack of specialist knowledge about firm's internal operations. Bozec and Bozec (2007) argued that NEDs are commonly part-time workers who undermine their ability to monitor and because of less information, advise the board only on what they have. This lack of information also reduces their ability to apply their decision efficiently. As a result, high levels of NEDs dominate boards and result in low quality decisions while also negatively impacting on firm performance. Previous studies Harmalin and Weisbach (1991); Hart (1995) also argued that NEDs often have lack of knowledge about the company, they do not bring the requisite skills to the job and are too engaged to contribute effectively. This might reduce their monitoring function to observe the managers who might work for their own interests rather than the interests of shareholders' and firm'. This will increase agency problem which leads to the negative impact on firm performance.

H2. There is a negative relationship between NED and firm performance.

4.3.3 Women Directors

Terjensen et al. (2009) showed that three key theories suggest greater gender diversity may further contribute to better board performance and effectiveness: agency theory, resource dependency theory and gender role theory. From the perspective of agency theory, Francoeur et al. (2008) suggest that women often bring a fresh perspective on complex issues which can help correct informational biases in strategy formulation and problem solving. Virtanen

(2012) study reports that female board members are more likely to take active roles on the board compared to their male board members.

There are other evidences of boards where more women have levels of public disclosure (Gul et al., 2011) and, better oversight of management reporting which enhances earnings quality (Srinidhi et al, 2011). Female board members attend more board meetings and are more prepared for board meetings (Adams and Ferreira, 2009). As such, it is expected to see a positive relationship between women directors and firm performance.

H3. There is a positive relationship between women director and firm performance.

4.3.4 Board Committees

Previous studies indicated that the number of committees in a board is also a significant measurement for firm performance. Boards are generally subdivided into smaller committees to observe the executive management efficiently and perform all other jobs which involves serious agency problems (McClogan, 2001). There are mainly three committees that support the board activities: audit, remuneration and nominations committees. These committees are comprised of expertise members who deal with specialised issues. McMullen (1996) found that firms that have audit committees face less financial distress. The study conducted by Klein (2002) mentioned that independent audit committees reduce the probability of earnings management which, in turn, increase transparency. On the contrary, Baxter (2010) found no relationship between firms' financial reports and the presence of audit committees. Weir and Laing (2000) argued that the presence of a remuneration committee leads to benefits for the firms and result in better performance. Similarly, Abbott et al., (2004) found that existence of

audit committees reduce the mistakes and abnormalities on the board. From the above literature it can be assumed that there is a positive relationship between board committees and firm performance.

H4. There is a positive relationship between Board committees and firm performance

4.3.5 Board Meeting

The intensity of a board's activities is measured by the frequency of board meetings, and the quality or effectiveness of its monitoring (Vefas 1999; Conger et al 1998). A higher frequency of board meetings leads to a higher quality of managerial monitoring, and therefore positively influences the financial performance (Vefas 1999; Ntim 2009). Frequent meetings with informal side-line interactions can create and strengthen cohesive bonds among directors (Lipton and Lorsch 1992), and will positively influence on corporate performance. Mangena and Taurigana (2008) found a positive relationship between the frequency of board meetings and firm performance. So it can be assumed that there is a positive relationship between frequency of board meetings and firm performance.

H5. There is a positive relationship between Board meetings and firm performance.

4.3.6 SSB Size

If the SSB is small, agency costs may be reduced and the coordination between the boards members may be increased (Quttainah et al., 2013). A smaller size also helps to get better communication, thus decisions making can be more effective (Yermack, 1996). Jensen

(1993) argues that there should be at least seven or eight people in the board to ensure effective performance. For the SSB, smaller size SSB is much easier to manage and monitor, compared to larger size SSB. There is also an argument supporting large SSB, as it may comprise of scholars with multi experience and skills and schools of *fiqh* which may then lead to a better understanding of the products and operation ultimately resulting in better performance (Hamza, 2016). Few empirical evidences confirm significant impact of SSB size on financial institution performance like Matoussi and Grassa (2012), Mollah and Zaman (2015) and Nomran et al. (2018). Thus, this study hypothesizes that:

H6. There is a positive relationship between SSB size and firm performance

4.3.7 Firm Size

Past studies have represented a positive impact of firm size on the financial performance (Black et al, 2006). On the contrary, some other previous studies have shown negative relationship. Larger size firms need more monitoring (Nenova, 2003) which also results in extra cost for the firms. When the size of the firm gets larger, the efficiency level gets low and the management losses its control on strategic and operational decisions. Finally, it is argued that large size firms have the higher possibility of meeting agency problems which will result in negative impact on firm performance.

H7. There is a negative relationship between firm size and firm performance.

4.4 Variables Definitions

Different studies have used different measurements to investigate the firm performance. Most of the empirical studies tried to examine the firm performance by applying some financial measures such as Tobin's Q (Yermack, 1996; Weir et al., 2002; Kiel and Nicholson, 2003), ROA (Yermack, 1996; Kiel and Nicholson, 2003), ROE (Bhagat and Black, 1999; Adjaoud et al., 2007), ROI (Adjaoud et al., 2007).

In this study, corporate governance variables are independent variables and firm performance variables are dependent variables in the regression and the accounting based measure which is ROA is used because it is the most common ratio used to measure firm performance (Adewale and Rahmon, 2014) and higher ROA shows higher firm performance (Al-Matari et al., 2014 and Habbash & Bajaher, 2015). Accounting based measures use audited accounting data that confirm more consistent and clear view towards firms and as a result, the market does not misrepresent these measures. Because they are based on book values, these measures are less volatile and more consistent than market based indicators like stock returns, share prices, etc. (Lopez et al., 2007). As the final financial performance variable, Tobin's Q which entails market value of equity is assigned to examine the firm performance from the market aspect. Further, it is believed that two measures are sufficient to a general picture of Malaysian financial institutions' performance. Although Haniffa and Hudaib (2006) argue that there is no certain result that indicates which measure is the best to examine firms' financial performance with. Hence, the ROA and Tobin's Q are defined as follows:

- $ROA = \frac{EBITDA}{Total\ Asset}$
- $Tobin's\ Q = \frac{Total\ Assets - Book\ Value\ of\ Equity + Market\ Value\ of\ Equity}{Total\ Assets}$

In turn, the independent variables are defined as follows:

- Size (SIZE) = In (Total Assets)
- Liquidity (LIQD) = $\frac{\text{Current Assets}}{\text{Current Liabilities}}$
- Leverage = Long-term Debt ($\frac{\text{Long-term Debt}}{\text{Book Value of Equity}}$)
- Board Size (Board_Size) = Number of total board members
- Non-Executive Director (NED) = Number of total non-executive members
- Women Directors (Women-Dir) = Number of total women board members
- Foreign Directors (Foreign_Dir) = Number of total foreign board members
- Company Age (C_Age) = the number of years since the company was established
- Board Committees = the number of board of directors' committee.
- Board Meetings = total number of meetings held annually.
- SSB Size (SSB_Size) = the size of SSB
- SSB Women members (SSB_Women) = the percentage of Women present in the Shariah Supervisory Board.
- SSB Qualification (SSB_Quali)= if any member with formal qualification in Business studies (Such as Diploma, bachelor, Masters, PhD) 1= Yes and 0= No
- SSB BOD (SSB_BOD) = Any SSB member sits on the board. 1= Yes and 0=No

Besides the dependent and independent variables, control variables were used to measure the firms' performance. There are different studies (Yermack, 1996 and Black et al., 2006) that have used different control variables to measure firm performance. In this study firm size and

firm age are used as control variables. This study used total assets as a proxy of firm size by using the natural logarithm of total assets. Firm size is used to measure its likely effect on financial performances of Malaysian firms. Firm age is calculated as each year minus establishment date of the company to determine how many years it had been incorporated before 2012, 2013, 2014, 2015 and 2016.

- Firm size (Size) = $\ln(\text{Total Assets})$
- Firm Age (C_Age) = the number of years since the company was established.

4.5 Data Sampling

The objective of this study is to conduct an investigation of the corporate governance practices of Malaysian financial institutions and their impact on the performance of these institutions. The aim is to compare between the firms with SSB and firms without SSB. The sample size of the study consists of Malaysian financial institutions listed for 43 of 50 companies. Banks and real estate investment trusts on the BNM and the MYX. However, the study sample was subject to the following criteria.

First, the study covers the years 2012-2016. The rationale for using this as the study period is summarised in the following points: (a) this study uses the Malaysian Corporate Governance Code 2012 and previous research papers as a guide for corporate governance variables (b) in Malaysia, the development of a comprehensive Islamic finance ecosystem was guided by two roadmaps. First one Financial Sector Masterplan (2001-2010), to ensure the effective

functioning of Islamic finance in parallel with the conventional banking and insurance. The second roadmap, the Financial Sector Blueprint (2011-2020), Malaysia aims to position itself as the premier global Islamic finance marketplace.

Ghauri and Gronhaug (2005) suggest that secondary data is an essential method and that there is no need to collect primary data if secondary data is available to answer the research questions. Therefore, this research used secondary data to measure corporate governance mechanisms and firm performance. Corporate governance mechanism variables and firm performance information were collected from Datastream, firms' annual reports, Malaysian Securities Market and Malaysian Financial Market websites. Data and information required for the study comprised of board size, liquidity, leverage, number of NEDs, board committees, board meetings, women board of directors, foreign directors, SSB size, percentage of women on the SSB and SSB members' qualifications. Performance data used in this study were ROA (Return on Assets) and Tobin's Q. The data on firm age was collected from the annual reports. Firms, for which no annual report or required information was available, were excluded from the current study.

Table 1: Summary of Research Data Set

Financial Institutions	No of Firms
Total financial institutions (18 Real Estate Investment Trusts) and (31 Banks)	50
Minus: Institutions, which do not have required information	(7)
Financial institutions with full data set	43

4.6 Testing Procedures

Data was analysed using Stata software to run data panels. This data panel regression uses the unbalanced panel data. Panel data analysis was not possible because of small sample size. This study employs OLS (Ordinary Least Square) with robust for heteroskedasticity.

Governance influence on firm performance (ROA and Tobin's Q) has been tested through linear regression models. To test the hypotheses, the following models are employed:

Full regression model:

In order to examine the relationship between governance variables and firm performance, the following model is developed.

Firm Performance = f (corporate governance variables, control variables)

Model 1:

Y_{it}

$$\alpha + \beta_1 \text{BODSIZE}_{it} + \beta_2 \text{NED}_{it} + \beta_3 \text{WOMENDIR}_{it} + \beta_4 \text{COMMITTEENO}_{it} + \beta_5 \text{MEETINGNO}_{it} + \beta_6 \text{FIRMSIZE}_{it} + \beta_7 \text{SSBSIZE}_{it} + \beta_8 \text{SSBWOMEN}_{it} + \beta_9 \text{SSBQUALI}_{it} + \varepsilon_{it}$$

Model 2:

Y_{it}

$$\alpha + \beta_1 \text{BODSIZE}_{it} + \beta_2 \text{NED}_{it} + \beta_3 \text{WOMENDIR}_{it} + \beta_4 \text{COMMITTEENO}_{it} + \beta_5 \text{MEETINGNO}_{it} + \beta_6 \text{FIRMSIZE}_{it} + \beta_7 \text{SSBSIZE}_{it} + \beta_8 \text{SSBWOMEN}_{it} + \beta_9 \text{SSBQUALI}_{it} + \varepsilon_{it}$$

Where, Y_{it} is alternatively ROA_{it} and Tobin's Q_{it} ,

BODSIZE_{it} is the board size for i th firm at time t .

NED_{it} is the non-executive director for i th firm at time t .

WOMENDIR_{it} is the number of women directors on the board for i th firm at time t .

FOREIGNDIR it is the number of foreign directors on the board for it h firm at time t .

COMMITTEENO it is the number of board committees for it h firm at time t .

MEETINGNO it is the number of board meetings for it h firm at time t .

FIRMSIZE it is the firm size for it h firm at time t .

SSBSIZE it is the SSB size for it h firm at time t .

SSBWOMEN it is the number of women in the SSB for it h firm at time t .

SSBQUALI it is the qualification of SSB members for it h firm at time t .

α is the intercept

β_i is the regression coefficient of it h variable and

$\epsilon_{i,t}$ is the composite error term

The subscript i represents the different firms and t represents the different years.

4.7 Summary

In this chapter, the research paradigm is considered and the research method used is described. Sample selections and all the dependent and independent variables with the control variables are introduced, research hypotheses are presented and data analysis techniques with the testing procedures are explained. The next chapter will analyse the research findings and present the discussion of the results from quantitative data (Datastream and annual report data).

Chapter 5: Data Analysis, Results and Interpretations

5.0 Introduction

The previous chapter explained the data and specified the research design employed in this study. This section aims to explore the main inferences which were drawn from the model regression. Section 5.1 starts with Descriptive statistics, continues with univariate analysis and multivariate analysis for dependent, independent and control variables. Univariate analysis is the simplest form of quantitative analysis which describes the single variable in terms of applicable unit of analysis: statistical dispersion, frequency distribution and central tendency. On the other hand, multivariate analysis refers to any statistical technique used to analyse data that arises from more than one variable. Multivariate analysis is continued in section 5.2. Then next section 5.3 of this chapter would be the Discussion.

The key purpose of this study is to find answers for seven research hypotheses which are:

- H1. There is a positive relationship between board size and firm performance.
- H2. There is a negative relationship between NED and firm performance.
- H3. There is a positive relationship between women director and firm performance.
- H4. There is a positive relationship between Board committees and firm performance
- H5. There is a positive relationship between Board meetings and firm performance
- H6. There is a positive relationship between SSB size and firm performance.
- H7. There is a negative relationship between firm size and firm performance.

In order to answer the research hypotheses, the study starts with the descriptive statistics to show mean, median, maximum and minimum, standard deviation, skewness and kurtosis values of variables to describe them separately. Then the ordinary least square was employed to establish if corporate governance indicators have an effect on company financial performance.

5.1 Univariate Analysis

The univariate analysis examines the predictive ability of independent variables one at a time.

5.1.1 Descriptive Statistics

The analysis begins with examining the basic features of the data using descriptive statistics. Table 2 represents 5 years summary of mean, median, maximum values, minimum values, standard deviation, skewness, kurtosis of dependent and independent variables from 2012 to 2016. The dataset of 213 observations from 43 companies during the time period of 5 years into the STATA, was recognised by the system as unbalanced data. This relates to the fact that all the financial institutions do not have complete data for all the years under observation. This study will start by comparing the performance of Malaysian financial institutions with SSB and without the SSB.

Table 2 compares and describes the performance and the perspective of assets growth of Malaysian financial institutions both with SSB and without SSB as a governance mechanism. Firstly, Board size (Board_Size) in descriptive statistics has an average of 7.47 with a

minimum of 4 and a maximum of 13. Jensen (1983) and Lipton and Lorsh (1992) recommend that the board size has a maximum of 7 to 8 members, with the maximum number of 10 to be effective. Mean of sample companies' board size support their suggestion with the number of 7.47. But the maximum number of board size from the descriptive statistics is 13, so this seems much higher than their findings. Most prior studies that investigated the impact of board size on firm performance found either a negative or a positive relationship. Dalton et al. (1999); Hillman and Dalziel (2003) and; argue that larger boards are better than the small ones in improving firm performance. They argue that in small boards the powerful position of the CEO enable him to override the decisions made by the board members in accordance with their own interests leading to increase the agency problem and correspondingly undermining the performance of the firm (Miller, 2003).

Table 2: Descriptive Statistics for 2012-2016

	Firms with SSB				Firms without SSB			
Variables	Mean	Min	Max	Std. Dev	Mean	Min	Max	Std. Dev
Independent variables (Governance variables)								
Liquidity	1.5220	0.1275	9.0609	1.9288	1.6212	.0086	14.1824	2.0068
Leverage	0.2360	0	0.5261	0.2129	0.2075	0	5.2506	0.4323
Board Size	9.2	6	13	1.8901	7.4702	4	12	1.8178
NED	7.6444	3	12	2.1758	5.625	1	11	1.9070
Women Director	1.5111	0	5	1.2177	1.0952	0	3	0.7679
Foreign Director	0.9111	0	4	1.4273	1.1845	0	6	1.5920
Committee No	4.6	3	8	1.0090	2.9583	0	8	1.259
Meeting No	11.8	4	25	4.7891	5.7559	2	21	3.0514
SSB Size	5.5555	3	9	1.5308	0	0	0	0
SSB Women	1.0444	0	3	0.8244	0	0	0	0
SSB Qualification	0.6444	0	1	0.4840	0	0	0	0
SSB BOD	0.0888	0	1	0.2877	0	0	0	0
Control variables								
Firm Size	17.6421	14.225	20.4166	1.9682	14.6337	11.9134	19.7558	1.6985
Firm Age	28.7777	6	56	16.1932	25.5	0	111	26.5232
Dependent variables (Performance variables)								
ROA (Return on Assets)	0.0240	-.0020	.0665	0.0153	0.1302	0	3.5462	0.3469
Tobin's Q	1.0468	0.8973	1.3445	.08969	1.0374	0.0199	3.1568	0.4536

The mean value of the proportion of non-executive directors of firms without SSB is 5.62 and a mean value of 7.64 for the firms with SSB as given in Table 2. The minimum number of non-executive directors is 1 and 3 whereas the maximum for the firms without SSB is 11 and for the firms with SSB is 12. This is consistent with some previous studies (Bhagat and Black, 1999; Yermack, 1996), which stated that higher percentages of NEDs in a firm are likely to experience poor performance because NEDs are not full-time workers, they are unfamiliar with business and operations and not able to comprehend the difficulties face by the firm.

Women directors has an average of 1.09 with the minimum of 0 and maximum of 3 for the firms without SSB and when it is with SSB the average is 1.51 with a minimum of 0 and maximum of 5 in Table 2. So the average of women directors on the board increases when the firm has SSB. The above table shows that there is a positive impact of women directors on the board. Different theoretical perspectives have positively supported the gender diversity in the boards. Erhardt et al. (2003) stated that agency theory is mainly concerned about monitoring the role of board of directors and emphasizing the representation from diverse groups will provide a balanced board so that no group of individuals or individual can dominate the decision making. On the other hand, a study conducted (Rose, 2007) shows insignificant association between proportions of women directors on the board and firm performance. However, it is now believed by many scholars that if there is an increase in gender diversity on the board then it may lead to better governance and allow the board to have broader talent pools (Bathula, 2008).

In Table 2, the average of board committees is 3 with the minimum of 0 and a maximum of 8 for the firms without SSB and in firms with SSB the average is 4.6 with a minimum of 3 and maximum of 8. The appointment of remuneration, audit and nomination committees by the firms are complying with the code of best practice on corporate governance.

Board meeting has the average of 5.7 with the minimum of 2 to maximum of 21 without SSB, while it has the average of 4.6 with minimum of 3 and maximum 8.

The mean value of SSB size is 5.5 with the range of 3 to 9 in the firms with SSB. Mollah and Zaman (2015) found mean size of SSB (4.17), ranging from 1 to 14 for a sample of 86 Islamic Banks across 25 countries. Firm size has an average of 15.26 with a range of 11.91 to 20.41.

5.1.2 Correlation Analysis

This analysis was used to test the study and understand the relationship among all the independent variables. Multicollinearity problem occurs when two or more independent variables are highly correlated with each other, which might have a negative impact on the regression (Hair et al, 2014). High correlation might make the regression unreliable. Table 3 exhibits pairwise correlation, which describes the correlation of independent variables related to this study.

Table 3: Correlation Analysis

	ROA	Tobin's Q	LIQD	Leverage	Size	C_age	Board_Size	NED	Women_Dir	Foreign_Dir	CommitteeNo	MeetingNo	SSB_Size	SSB_Women	SSB_Quali	SSB_BOD
ROA	1															
Tobin's Q	-0.2834***	1														
LIQD	0.0611	0.0088	1													
Leverage	-0.0574	0.1490 **	-0.0987	1												
Size	-0.2593***	0.1344	-0.2197***	0.1291	1											
C_age	-0.1223*	0.1088	0.0146	-0.0973	0.3013***											
Board_Size	-0.0869	0.2100***	-0.1296	0.1333	0.5871***	0.1086	1									
NED	-0.0878	0.2301***	-0.0688	0.0457	0.5036***	0.1245*	0.7434***	1								
Women_Dir	-0.0365	0.0857	-0.1992***	-0.0329	0.3535***	0.0357	0.3800***	0.3317***	1							
Forein_Dir	-0.1003	0.0729	-0.2141***	0.1431**	0.1891***	-0.0387	0.4187***	0.2567***	0.088	1						
CommitteeNo	-0.0475	0.009	-0.0605	0.0412	0.3554***	0.1617	0.1926***	0.1854***	0.2100***	-0.0837	1					
MeetingNo	-0.1327	0.1879***	-0.0876	-0.0316	0.7026***	0.2846***	0.3152***	0.3825***	0.1231*	-0.1091	0.3621***	1				
SSB_Size	-0.1370**	0.0039	-0.0322	0.0333	0.6128***	0.0725	0.3673***	0.3356***	0.1822***	-0.0212	0.4746***	0.6135***	1			
SSB_Women	-0.11	0.01	-0.0995	-0.0179	0.4943***	0.1161**	0.3244***	0.3606***	0.1704	0.0215	0.3458***	0.5818***	0.7770***	1		
SSB_Quali	-0.112	0.0017	0.0139	-0.0671	0.4393***	0.0519	0.1733	0.1644	0.1945***	-0.1027	0.3092***	0.4953***	0.8193***	0.6898***	1	
SSB_BOD	-0.0306	-0.0439	0.2679***	-0.0461	0.0197	0.0859	0.0116	0.0781	-0.1446**	-0.1002	0.17	0.0639	0.2815***	0.1290*	0.3485***	1

Note: *, ** and *** indicate 10%, 5% and 1% level of significance, respectively

As shown above, board size has a positive relationship with SSB size (0.3673), firm size (0.5871) and firm age (0.1086), women director (0.3800), number of committees (0.1926), NED (0.7434). NED is positively correlated with board committees (0.1854), firm size (0.5036) and firm age (0.1245). Board committees are positively related with firm size (0.3554) and firm age (0.1617). Firm size has a positive association with firm age (0.3013), leverage has a positive association with firm size (0.12).

The highest correlation is between SSB size and the qualification of SSB members. SSB size and female members in the SSB is the second highest correlation. Our results show that women director has a positive relationship with Tobin's Q.

5.2 Multivariate Analysis

Multivariate analysis uses different variables to test the association between corporate governance variables and firm performance. The multiple regression models have been used in previous corporate governance and firm performance studies such as Vafeas (1999).

5.2.1 Ordinary Least Squares (ROA)

Table No 4

Variables	Main Variables		Main with Interactive Variables		Interactive Variables only	
	Coef.	Std. Err.	Coef	Std. Err.	Coef	Std. Err.
ROA						
LIQD	.0003	.0105	.0011	.0105		
Leverage	-.0164	.0188	-.0147	.0166		
Size	-.0573**	.0277	-.0563**	.0272		
C-age	.0007	.0003	-.0009**	.0004		
Board_Size	.0252	.0136	.0233*	.0137		
NED	-.0055	.0064	-.0064	.0072		
Women_Dir	.0160	.0197	.0759	.0487		
Foreign_Dir	-.0148	.0094	-.0182*	.0108		
CommitteeNo	.0077	.0092	.0419*	.0252		
MeetingNo	.0087**	.0038	.0074**	.0035		
SSB_Size	.0018	.0093	-.0552**	.0255		
SSB_Women	-.0085	.0159	-.0044	.0165		
SSB_Quali	-.0342	.0344	.0260	.0380		
SSB_BOD	-.0486	.0420	-.0623	.0425		
Board_Size x SSB_Size			.0048**	.0024	-.0017*	.0005
Women_Dir x CommitteeNo			-.0182*	.0103	-.0003	.0029

Note: *, ** and *** indicate 10%, 5% and 1% level of significance, respectively

Table no 4 shows the regression results for ROA. The first column shows the coefficient of all independent variables that shows the magnitude and direction of relation between

independent variables and financial performance measure (ROA). The second column represents the standard errors and the third column shows the t-value, which states the significance of the regression outcomes. When it comes to the comments from the analysis, findings from OLS regression clearly indicates mixed results between independent variables and ROA.

Liquidity, board size, women director, number of committees, number of board meetings and SSB size all have positive impact on the financial measurement (ROA). On the other hand, firm size, leverage, NED, firm age, SSB women, qualification of SSB members, and number of SSB members sit on the board shows negative association with the financial measurement (ROA). However only firm size, board size, firm age and number of board meetings have significant impact on ROA. More specifically, double-size firms will experience approximately 6% reduction in ROA while mature firms experience slightly higher ROA. Larger board size improves ROA performance by 3% and more frequent meetings also improve performance slightly.

In this study two pairs of interactive variables have been tested to measure their influence of firm performance. The table shows that first interactive variable which is $\text{Board_Size} \times \text{SSB_Size}$ has positive and significant effect on ROA. The second interactive variable which is $\text{Women_Dir} \times \text{CommitteeNo}$ shows negative but significant impact on ROA. These two results are particularly interesting as they demonstrate the joint effect of the governance factors in influencing the firm's performance. A synergy between board and SSB members will slightly improve ROA performance while negative performance is observed for having more women directors in the committee.

5.2.2 Ordinary Least Squares (Tobin's Q)

Table No 5

Variables	Main Variables		Main with Interactive Variables		Interactive Variables only	
	Coef.	Std. Err.	Coef	Std. Err.	Coef	Std. Err.
Tobin's Q						
LIQD	.0100	.0169	.0104	.0168		
Leverage	.1858***	.0635	.1927***	.0646		
Size	-.0373	.0338	-.0362	.0334		
C-age	.0013	.0011	.0014	.0011		
Board_Size	.02837	.0325	.0402	.0344		
NED	.0293	.0185	.0228	.0188		
Women_Dir	.0204	.0359	.0584	.0663		
Foreign_Dir	.0113	.0118	.0106	.0127		
CommitteeNo	-.0058	.0159	.0010	.0345		
MeetingNo	.0333	.0134	.0325	.0135		
SSB_Size	-.0350	.0148	.0650	.0571		
SSB_Women	-.1025*	.0592	-.0809	.0571		
SSB_Quali	.1899**	.0867	.0712	.0917		
SSB_BOD	-.1586	.1048	-.1810*	.1005		
Board_Size × SSB_Size			-.0098	.0050	-.0001	.0006
Women_Dir × CommitteeNo			-.0078	.0140	.0033	.0050

Note: *, ** and *** indicate 10%, 5% and 1% level of significance, respectively

5.2.2 Ordinary Least Squares (Tobin's Q)

Table no 5 shows the regression results for Tobin's Q. It is found that board size, NED, women director, number of board meetings and liquidity all has positive impact on the firm's market performance. On the other hand, firm size, SSB size, SSB women, number of SSB members sit on the board shows negative association with the firm's market performance. Interestingly, it is found that the firm's market performance is affected by a set of different factors as compared to the previously analysed ROA performance. Leverage, number of board meetings, SSB size, women SSB and qualification of the SSB members have significant impact on firm's market performance. More specifically, 10% increase in leverage will improve firm's market value by approximately 2% and more frequent meetings improves market value by 3%. Interestingly, larger SSB size and the presence of women in SSB reduce market performance by 4% and 10%, respectively. Market performance is observed to be increased by 19% for SBB with more qualifications. In terms of the effect of interactive factors on firm's market performance, this study only found a slightly reducing market value performance causing by an interaction between the Board_Size and the SSB_Size.

The summary of the hypotheses results with regard to the relationship of governance and performance variables are given in Table 6

Table 6: Summary of Hypotheses Results

Financial Measurement	Independent Variable	Relationship Direction	Significant Value	Result on Hypothesis
ROA	Board_Size	Positive	0.067*	Reject H1
Tobin's Q	Board_Size	Positive	0.384	Accept H1
ROA	NED	Negative	0.373	Accept H2
Tobin's Q	NED	Positive	0.115	Accept H2
ROA	Women_Dir	Positive	0.384	Accept H3
Tobin's Q	Women_Dir	Positive	0.561	Accept H3
ROA	CommitteeNo	Positive	0.872	Accept H4
Tobin's Q	CommitteeNo	Negative	0.716	Accept H4
ROA	MeetingNo	Positive	0.023*	Reject H5
Tobin's Q	MeetingNo	Positive	0.014*	Reject H5
ROA	SSB_Size	Positive	0.646	Accept H6
Tobin's Q	SSB_Size	Negative	0.019*	Reject H6
ROA	Size	Negative	0.040*	Reject H7
Tobin's Q	Size	Negative	0.271	Accept H7

*: Significant impact

** : Statistically significant impact

5.3 Discussion

This section deals with the main implications, which were drawn from the regression models. We are going to consider that the results are highly significant at 0.01, significant at 0.05 and marginally significant at 0.1, which applies to all of the following tables and results.

Firstly, we found that when the board size increases, the ROA and Tobin's Q also increases. Simon et al. (2014) and Mohamed (2009) found a positive relationship between board size and financial performance for Malaysian companies. The board size has significant effect on ROA but it has insignificant effect on Tobin's Q. However, there are some advantages of having larger boards. Dalton et al. (1999) suggested that larger boards offer high quality advice and counsel to the CEO. Furthermore, large board perform their strategic function more effectively, which is essential during periods of financial turbulence to reduce agency problems (Mintzberg, 1983).

The study shows that there is a negative relationship between NED and firm performance in terms of ROA, and positive in terms of Tobin's Q but still statistically insignificant relationship of NED and firm performance. Additionally, NEDs might not be independent enough to perform their job and effectively monitor or they are unable to interfere in management decision because of close relationships with managers sometimes. In line with stewardship theory, NEDs are less capable of monitoring the managers than inside directors because of their lack of specialist knowledge about firm's internal operations.

When the number of board committees increase, ROA also increases while the Tobin's Q decreases. Number of committee members is an important variable for corporate governance, so if it increases that means there is an increase in better supervision of decision, disclosure of information and better protection of rights. Overall it proves the quality of better corporate governance and has a positive impact on firm performance. However these relationships are not significant for ROA and Tobin's Q. When we compare the finding with past studies, there are some of the findings that support the presence of different board committees for increasing firm performance. McMullen (1996) found that increasing the number of board committees ensures that the firms have powerful internal audit which results in less stressed financials. Klein (1998) also found a positive relationship between board committees and firm performance though it is not significant. The reason for this insignificance may be that the committee members are not independent enough and firms should give importance to their independence level. According to Lam et al. (2012), the efficiency of the board committees depends on the independence of the board composition.

Results show that there is a positive relationship between number of board meetings and firm performance and it has also significantly affects both ROA and Tobin's Q. Frequency of board meetings is positive but insignificant on both performance measures. The result is consistent with Vefas (1999) who reported a negative relationship between frequency of board meeting and financial performance using Tobin's Q as a performance proxy.

The sample of this study shows that women directors on the board have positive but insignificant relationship with both ROA and Tobin's Q.

According to the results SSB size has a positive but insignificant association with ROA while it shows a negative and significant relationship with Tobin's Q. According to the findings of ROA, the size of SSB enhances the firm performance but the result from Tobin's Q shows that the smaller the SSB size the better the firm performance.

Firm size is negative and significant according to ROA, suggesting that smaller companies in the sample are the ones who are performing best. The findings of Tobin's Q show a negative and insignificant relationship between firm size and firm performance.

Result from this study shows that leverage reports a negative and highly insignificant impact on financial performance (ROA): higher levels of debt will decrease firm performance. In other words, the findings indicate that the higher the debt ratio, the lower the ROA. The reason for higher level of debt ratio in firms might be the increase in cost of operations (Dechow et al. 1996). Higher debt ratio may result in firm's inability to raise new credit and also the reason for losing valuable investment opportunities. This also refers to the negative impact of higher debt ratio on the amount of dividends paid. In addition, higher leverage shows financial distress.

5.4 Summary

This chapter discussed the empirical findings regarding the impact of corporate governance mechanisms, particularly the impact of SSB on firm performance. The chapter specifically presented the discussion and the findings of the descriptive analysis undertaken in this study, and dealt with the main inferences drawn from the multiple regressions. The tables are presented separately according to the research objectives in order to ensure that the discussion and the presentation of the findings are straightforward.

Chapter 6: Summary and Conclusion

6.0 Introduction

This concluding chapter is organised as follows. Section 6.1 provides the summary of the analysis performed. Next section 6.2 discusses the conclusion. Section 6.3 discusses the limitations of the research, and the last section 6.4 recommends avenues for future research.

6.1 Summary

The review of different corporate governance theories refers to the importance of board of directors as an essential part of internal governance that monitor the management to achieve the business objectives successfully and also enhance the companies' performance. The aim of this study was to determine the relationship between corporate governance mechanisms and firm performance and in particular the impact of SSB on the firm performance. This was achieved through defining the governance variables and two performance measures (dependent variables).

This section summarises the results, in context of the research questions initially set out.

Research question 1

Is there any relationship between corporate governance mechanisms and the Malaysian financial institutions' performance?

This study found some evidence to suggest that there is a relationship between corporate governance mechanisms and the Malaysian financial institutions' performance. Very interestingly, the evidence suggests a positive effect on firm's performance. More specifically, it is found that the frequency of board meetings, the proportion of women directors in the board and the number of committees on the board are positively related with firm's performance. This is sensible because those factors signify improved corporate governance practice. The benefit of improved governance can be in the form of possible reductions in the firms' cost of capital that subsequently improves their firm's value. A positive relationship between the board size and ROA supports the view that Malaysian financial institutions with larger boards may provide for more efficient monitoring of the current activities of the firm.

Research Question 2

Is there any similarity and difference between the performance of firms' with SSB and firms' without SSB?

This study found differences between the performance of firms with and without SSB. To certain extent, there is some evidence to suggest that firms without SSB perform better. This is particularly interesting in the case of Malaysian financial institutions because there are some Islamic financial institutions that do not have a SSB or a Shariah advisor. Despite SSB is commonly regarded as a compulsory structural component and legitimate body of authority for an Islamic financial institution, its effect on the overall institutional performance is rather far from being prevalent.

Research Question 3

Is there any reason behind the absence of SSB in Islamic financial institutions despite of the requirement?

There are some reasons behind the absence of SSB in the Malaysian Islamic financial institutions even though it is a requirement for them. SSB in Islamic financial institutions are not much powerful and well-equipped to regulate operations of individual institutions.

Indispensably however, such a regulatory body could have been armed with some powers of exercising punitive measures within the meaning of executive functionality.

In the Islamic financial institutions, Shariah scholars or experts certify what is permissible and ensure the firm's activities work in compliance with Shariah. However, there is evidence of shortage of Shariah scholars where there are scholars working in more than one firm. This affects the firm's performance negatively as well as raises a question on transparency and accountability of the scholars. In the present governance structure of Malaysian financial institutions, this study found that SSB is not contributing adequately.

6.2 Conclusion

The results of this study report that good corporate governance is an important factor in determining firm performance. Many inferior performance and business failures are due to the board's inability to address the overall company performance in an effective manner. The reason is in the structure of the board, particularly in relation to the structure of the decision making process which needs to be reformed to focus on sustaining high performance in the face of a rapidly changing environment (Cutting & Kouzmin 2000). Therefore, governance structures must be designed to improve the quality of monitoring of board decisions (Laing & Weir 1999). It can also be argued that firms which have implemented effective governance practices consisting of the board structures recommended in the code of best practice in Malaysia are likely to adopt strategies that will result in long-term sustainability of the firms.

This study examined corporate governance variables which are board size, non-executive director, women director, board meetings, board committees, SSB size and investigated the

effect of these variables on firm performance, while controlling for firm's size and age factors. Building upon corporate governance theories of agency and stewardship, it can be concluded that board's monitoring is pertinent in achieving positive performance while the SSB's stewardship role does not contribute to firm's performance.

6.3 Limitations of the Study

This study has some limitations. First, the data collection was limited to publicly available data sources such as annual reports and other databases. If there are problems relating to data disclosures or professional accounting practices, then that would limit the validity of the findings. The use of secondary data for this study also limits the opportunity to gather some specific information needed to analyse other dimensions such as the qualitative characteristics of the shareholders, board and SSB members.

Second, the entire population comprises of only 43 Malaysian financial institutions, which is relatively smaller sample. The size of the sample is limited by number of firms listed on the Malaysian stock exchange in year 2012-2016.

Only secondary data used for this study, limited the chances to gather some specific information needed to analyse certain information such as, shareholders, board members and SSB members. Third, this study is strictly quantitative and based on only one stock market. The financial performance indicators are also limited to ROA and firm's market value as measured by Tobin's Q.

6.4 Suggestion for Further Research

This study makes a considerable contribution to the understanding of corporate governance practice in Malaysia and its role in influencing the firm's performance. While this study focuses on listed companies in the BNM and MYX, it is also important to understand the corporate governance practice in the non-listed companies of Malaysia. The future research could be in the form of a comparative assessment of corporate governance practices between listed and non-listed companies in Malaysia. This will offer an avenue to examine whether the practices are affected in a similar fashion or otherwise.

This study was undertaken from 2012 to 2016, so future research could examine corporate governance practices and firm performance by exploring a longer period to provide an in-depth understanding of the relationship between corporate governance practices and firm performance. Moreover, it is also recommended that future studies investigate more governance mechanisms to test their relationship with firm's performance.

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Appendix

Table 7: List of Financial Institutions used in this research

No	Name of Financial Institutions	Sector
1	Amanah Harta	REIT
2	Al-Aqar	REIT
3	AmFirst	REIT
4	Amanahraya	REIT
5	Atrium	REIT
6	Axis	REIT
7	Capitaland	REIT
8	Hektar	REIT
9	IGB	REIT
10	KLCC PROPERTY HOLDINGS BERHAD	REIT
11	MRCB-Quill	REIT
12	Pavilion	REIT
13	Sunway	REIT
14	Tower	REIT
15	UOA	REIT
16	YTL	REIT
17	AEON	FINANCE
18	Affin	FINANCE
19	AMMB	FINANCE
20	Apex	FINANCE
21	BIMB	FINANCE
22	Bursa	FINANCE
23	CIMB	FINANCE
24	ECM Libra	FINANCE

25	ELK Desa	FINANCE
26	Hong Leong Bank	FINANCE
27	Insas	FINANCE
28	Johan	FINANCE
29	LPI Capital	FINANCE
30	MAA	FINANCE
31	Manulife	FINANCE
32	Malayan Banking	FINANCE
33	M Building Society	FINANCE
34	MNRB	FINANCE
35	MPHB Capital	FINANCE
36	OSK	FINANCE
37	P&O	FINANCE
38	PB Bank	FINANCE
39	RCE Capital	FINANCE
40	RHB Bank	FINANCE
41	TA Enterprise	FINANCE
42	Syarikat Takaful	FINANCE
43	Tune Project	FINANCE