The impact of corporate governance mechanisms on institutions finance and credit from Europe

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Please cite this paper as:
Ladaru, R.G., Troaca, V.A. Andrei, Valeriu I.A.,and Cosma,R.M, 2024. The impact of corporate governance mechanism on institutions finance and credit from Europe, In: R. Pamfilie, V. Dinu, C. Vasiliu, D. Pleşea, L. Tăchiciu eds. 2024. *10th BASIQ International Conference on New Trends in Sustainable Business and Consumption*. Almeria, Spain, 6-8 June 2024. Bucharest: Editura ASE, pp. 105-110
DOI: 10.24818/BASIQ/2024/10/025

Abstract

Purpose/objectives: The purpose of this study is to examine the corporate governance of companies at the level of some European states through a systematic review of the literature, but also through an econometric analysis.

Design/methodology: The methodological approach is based on a set of methodological tools, which combines fundamental research with quantitative research and modern methods with classical methods. The complex character of the topic requires the configuration of the appropriate methodology- the establishment of objectives, directions, hypotheses and methods- essential in the development of a quality research.

Findings: A negative relationship was identified between ROE and gender diversity, board independence and audit committee existence, and a positive relationship with audit committee independence.

Originality/value: This study adopted an explanatory research design, and secondary data were collected and analyzed by independent samples t-tests and group statistics using SPSS software.

Possible practical implications: The research covered by this paper has an applied importance, given the fact that it presents the accounting information from the perspective of the primary source of data for the analysis of financial performance.

Keywords

companies, corporate governance, credit, finance

DOI: 10.24818/BASIQ/2024/10/025

Introduction

Corporate financial reporting provides fundamental information to a wide range of policy makers in both the corporate and non-corporate sectors of the econom- shareholders, management, government, creditors, and society at large (Popescu et al., 2018, Balu et al., 2019). This information is a vital input for effective and efficient management and requires attention in practices (Aguilera& Crespi-Cladera, 2016). More specifically, a dynamic and competitive financial institution environment requires improved observation, measurement and transparent disclosure of operations (Borisova et al., 2012).

The wave of corporate scandals involving famous companies in Europe and the USA (eg LEHMAN BROTHERS, etc.) has raised questions about what composition of the board of directors can best monitor and control the activities of management (Teixeira&Carvalho, .2024).

The management of these companies was involved in dubious, dubious and fraudulent accounting practices, and their boards of directors could not detect them in time. Fraud, mismanagement and poor monitoring of agents' activities have led to a lack of transparency and accountability, making these top companies vulnerable to failure (Elbahar et al., 2021).

Modern businesses characterized by frenzied turbulence amid the crushing speed of globalization and technology, hyper-competition, disruptive pace of financial innovations, rejuvenated wave of international acquisitions and mergers, have a heightened need for efficiency, stability and sustainability (Boubakri et al., 2018, Calin et al., 2022).

In this paper, we aimed to present the main aspects that analyze corporate governance, represented by variables such as: the size of the board of directors, gender diversity, the existence of the audit committee and the independence of the audit committee, and the financial performance of the institutions financial and credit in Europe, represented by market values (Tobin Q rate) and accounting values.

Review of the scientific literature

The relationship between board size and the financial performance of companies has been widely debated over time. Board size is generally calculated as the number of board members while financial performance is generally measured by return on assets (ROA) and return on equity (ROE).

Agrawal and Lakshmi (2020) determined in their study the impact of Board composition (proportion of non-executive directors) and Board size on the financial performance of companies. The study used group data of 145 companies for a period of five years and used panel linear regression model to study the relationship between different variables. The study also concludes a positive relationship between non-executive directors and company financial performance because these directors bring their expertise, network and resources to the organization, which is crucial for the growth and performance of the company.

Lee-Kuen et al. (2017) analyzed the interdependence between board gender diversity and the financial quality of listed firms. on Bursa Malaysia for the period 2009 to 2013. Using unbalanced panel data analysis, they tested whether board gender diversity can influence firm performance as measured by by Tobin's Q. They used four different indicators for gender diversity (the dummy variable for women, the percentage of women on the board, the Blau index and the Shannon index) to provide a more comprehensive measure of gender diversity. This study suggests that a higher degree of female representation on the board of directors increases a firm's financial performance. Positive discrimination favoring the appointment of women to the board is therefore likely to persist as a feature of the corporate governance landscape in Malaysia.

Jabari and Muhamad (2021) analyzed the influence of gender diversity among board of directors (BOD) and Shariah supervisory board (SSB) members on the financial performance of Islamic banks in Indonesia and Malaysia. Data for a sample of 19 Islamic banks for the period 2010-2018 were collected to test the research hypotheses using ordinary least squares estimation. The generalized least squares estimation method was used to confirm that the results are robust. Consequently, the researcher developed a multiple linear regression model to investigate the nature of this relationship, whereby return on assets (ROA) was used to measure the performance of Islamic banks listed in the Gulf Cooperation Council, covering the period between 2013 and 2016. The results indicated a negative relationship between board structure and performance of Islamic banks.

Research methodology

As working methodology, we insisted on two approaches frequently used in fundamental analysis: the literature review and the regression analysis. Based on the specialized literature, the results of the studies from the last years that targeted these aspects were reviewed and research hypotheses were developed. Regression analysis, descriptive statistics and correlation matrices were used to analyze the impact that corporate governance can have on companies' performance.

Results and discussion

Data on corporate governance and bank performance mechanisms were collected from the Refinitiv Eikon database for all European public and private financial institutions available in the database. The data was collected for the period 2019-2022. Those companies that did not present information on corporate governance were removed from our sample, so the distribution of companies included in our study is shown in Table 1.

Tab1e 1. Distribution of the sample according to the activity sector

Year / *Economic sector*	*2022*	*2021*	*2020*	*2019*	*Total*	*Percentage of total*
Banks	81	75	66	59	281	41%
Capital markets	48	39	34	25	146	21%
Consumer financing	10	10	8	4	32	5%
Diversified financial services	12	12	10	7	41	6%
Insurance	46	46	43	40	175	26%
Savings and mortgage financing	3	3	3	2	11	2%
General	*200*	*185*	*164*	*137*	*686*	*100%*

Source: own processing

More than half of our sample is concentrated in six countries: the United Kingdom, representing 19% of the sample, Switzerland with 13%, Italy with 10% and Germany with 9%, Poland and France with 8% each.

Financial performance is our dependent variable, which will subsequently take the value of return on assets (ROA) and the value of return on equity (ROE) as well as the market value of companies, measured by the Tobin Q rate.

The independent variables are corporate governance mechanisms. The variables analyzed are: board size (BZ), board independence (BI), gender diversity (BG), audit committee existence (CA) and audit committee independence (CAI). In the first part of our analysis we will analyze the descriptive statistics of the sample, Pearson and Spearman correlation to have a broad picture of the variables included in our study.

Table 2. Pearson's correlation matrix

Variables	*BZ*	*BG*	*BI*	*AC*	*ACI*	*Tobin Q*	*ROE*	*ROA*	*FZ*	*LV*
BZ	1	,172**	-,138**	,150**	-0,006	-,228**	-,169**	-,130**	,566**	-,277**
BG	,172**	1	,130**	0,068	,100**	-0,064	-,079*	-,089*	,233**	0,022
BI	-,137**	,130**	1	,156**	,721**	0,063	-0,042	-0,003	,124**	-0,010
AC	,150**	0,068	,158**	1	0,020	-,098*	-0,071	-,098**	,144**	-,085*
ACI	-0,006	,100**	,721**	0,020	1	,118**	-0,005	,080*	,124**	-,088*
Tobin Q	-,228**	-0,065	0,063	-,098*	,119**	1	,400**	,450**	-,512**	0,066
ROE	-,169**	-,078*	-0,041	-0,071	-0,005	,400**	1	,550**	-,167**	0,063
ROA	-,130**	-,089*	-0,002	-,099**	,080*	,450**	,550**	1	-,267**	-0,008
FZ	,566**	,233**	,124**	,144**	,124**	-,512**	-,167**	-,267**	1	-,259**
LV	-,277**	0,024	-0,010	-,086*	-,088*	0,066	0,063	-0,008	-,259**	1

The table above shows the Pearson's correlation matrix that measures the statistical relationship and association between the dependent, independent, and control variables included in our sample. It can be seen that the size of the board of directors is strongly negatively correlated with the Tobin Q rate at the 0.01 level, as well as with the accounting-based variables ROE and ROA.

Gender diversity is negatively associated with the Tobin Q rate but insignificantly. In contrast, gender diversity is strongly significant and negative with ROA and ROE at the 0.05 level. Board independence is negatively associated with our dependent variables ROA and ROE, with the Tobin Q rate being positively associated but statistically insignificant.

Table 3. Spearmen correlation matrix

Variables	*BZ*	*BG*	*BI*	*AC*	*ACI*	*Tobin Q*	*ROE*	*ROA*	*FZ*	*LV*
BZ	1	,116**	-,189**	,128**	-0,026	-,346**	-,221**	-,199**	,580**	-,175**
BG	,116**	1	,106**	0,048	,087*	-0,021	-0,052	-0,015	,178**	,108**
BI	-,189**	,105**	1	,098*	,652**	-0,021	-0,060	-0,068	,105**	,100**
AC	,128**	0,047	,098*	1	0,042	-0,008	-0,014	-,112**	,130**	-0,040
ACI	-0,026	,088*	,651**	0,042	1	-0,014	0,036	-0,005	,114**	-0,036

Tobin Q	-,346**	-0,021	-0,021	-0,008	-0,012	1	,472**	,687**	-,696**	,153**
ROE	-,221**	-0,051	-0,060	-0,015	0,036	,472**	1	,646**	-,223**	,085*
ROA	-,199**	-0,014	-0,068	-,112**	-0,006	,687**	,646**	1	-,446**	,113**
FZ	,580**	,178**	,105**	,130**	,114**	-,696**	-,224**	-,446**	1	-,143**
LV	-,175**	,108**	,100**	-0,040	-0,036	,153**	,085*	,113**	-,143**	1

The Spearman correlation matrix for all variables included in this study was presented in Table 3. The Tobin Q rate is negatively correlated with all our independent variables all at a significant level. A significant and negative correlation at the 0.01 level was identified in its relationship with board size. Return on assets is strongly negatively correlated with board size at the 0.01 level and with the other variables a negative correlation was identified, except for board independence where a positive correlation was identified. A strong negative correlation at the 0.01 level was identified between the size of the board of directors and the existence of the audit committee. A negative correlation was also identified between gender diversity and audit committee independence. A positive correlation was identified between audit committee independence and return on assets.

The table below shows the impact that corporate governance mechanisms have on the performance of financial and credit institutions represented by return on equity. It can be seen that our independent variables explain about 2.5% of the variation in the dependent variable return on equity.

Table 4. The impact of corporate governance mechanisms on ROE

Variables	*B*	*Sig.*	*B*	*Sig.*	*B*	*Sig.*	*B*	*Sig.*	*B*	*Sig.*
BZ	-0,365	0,019								
BG			-0,049	0,201						
BI					-0,011	0,581				
AC							-3,429	0,287		
ACI									0,009	0,603
FZ	-0,648	0,024	-0,909	<,001	-0,962	<,001	-0,939	<,001	-1,034	<,001
LV	0,001	0,975	0,013	0,592	0,010	0,687	0,008	0,753	0,006	0,818
(Constant)	31,795	<,001	35,472	<,001	35,971	<,001	38,110	<,001	36,354	<,001
Anova	<,001b		<,001b		<,001b		<,001b		<,001b	
F	6,544		6,544		6,086		6,372		6,914	
Adjusted R Square	0,026		0,026		0,025		0,025		0,028	

It can be seen that board size negatively and statistically significantly influences return on assets at the 0.05 level. So our first hypothesis is rejected by 33.33%. Board gender diversity has a negative and statistically insignificant impact, thus our second hypothesis is rejected by 33.33%. Board independence has a negative and statistically insignificant impact at the 0.01 level, thus our third hypothesis is rejected by 33.33%.

The existence of the audit committee negatively influences the rate of return on equity, but from a statistical point of view it is insignificant, thus the fourth hypothesis is rejected in proportion of 16.67%. Board independence has a positive and statistically insignificant impact, thus our fourth hypothesis is accepted in proportion to 16.67%.

Table 5. The impact of corporate governance mechanisms on ROA

Variables	*B*	*Sig.*	*B*	*Sig.*	*B*	*Sig.*	*B*	*Sig.*	*B*	*Sig.*
BZ	0,017	0,715								
BG			-0,006	0,578						
BI					0,006	0,372				
AC							-1,385	0,075		
ACI									0,015	0,005
FZ	-0,532	<,001	-0,507	<,001	<,001	<,001	<,001	<,001	<,001	<,001

LV	-0,015	0,036	-0,015	0,035	-0,016	0,028	-0,016	0,023	-0,010	0,145
(Constant)	14,594	<,001	14,344	<,001	<,001	<,001	<,001	<,001	<,001	<,001
Anova	<,001[b]		<,001[b]		<,001[b]		<,001[b]		<,001[b]	
F	19,225		19,292		19,468		20,335		16,934	
Adjusted R Square	0,074		0,074		0,075		0,078		0,067	

Board size positively and statistically insignificantly influences return on assets at the 0.05 level. So our first hypothesis is accepted in proportion of 33.33%. Board gender diversity has a negative and statistically insignificant impact, thus our second hypothesis is rejected by 33.33%. The independence of the board of directors has a positive and statistically insignificant impact at the 0.01 level, thus our third hypothesis is accepted in proportion of 33.33%. The existence of the audit committee negatively influences the return on assets, but from a statistical point of view it is insignificant, thus the fourth hypothesis is rejected in proportion of 16.67%. Board independence has a positive impact.

Table 6. Acceptance of assumptions

Variables	*Tobin Q*	*ROE*	*ROA*	*% Assumption*
BZ	+	-	+	67%
BG	+	-	-	33%
BI	+	-	+	67%
AC	-	-	-	0%
ACI	+	+	+	100%

The first hypothesis is accepted by 67%, which translates to 67% that more board members help companies perform better. The second hypothesis is accepted by 33%, which can be interpreted that more women on boards helps to achieve performance only when approaching performance on market values and not on accounting values.

The third hypothesis is accepted by 67%, which translates to 67% that more independent board members help companies achieve better performance. Thus the existence of the audit committee has a negative impact on our dependent variables, while the independence of the audit committee has the exact opposite impact.

Conclusions

This paper addressed the relationship between corporate governance mechanisms and the performance of financial and credit institutions in Europe. Corporate governance is a well-known target for academic research. because it has a special effect on the company. Shareholders, management remuneration, corporate governance policies and social networks are the most important research topics in this regard.

Corporate governance has recently been the subject of major political decisions and a very popular issue in the media in all countries, in the context of its potential role in increasing shareholder value and firm performance. The amount of corporate scandals and frequent cases of mismanagement, proprietary trading activities and the resulting dilution of trust in corporate systems have led regulators, corporations and stakeholders to re-emphasise the need for strict governance norms and practices. As a result, renewed attention of researchers and organizations has been directed towards analyzing the impact of corporate governance on firm performance and stability.

The first hypothesis is accepted by 67%, which translates to 67% that more board members help companies perform better. The second hypothesis is accepted by 33%, which can be interpreted that more women on boards helps to achieve performance only when approaching performance on market values and not on accounting values. Our third hypothesis is accepted by 67%, which translates to 67% that more board members who are independent help companies achieve better performance.

The last hypothesis took into account two variables: the existence of the audit committee and the independence of the committee. Thus the existence of the audit committee has a negative impact on our dependent variables, while the independence of the audit committee has the exact opposite impact.

Further studies on corporate governance in Europe are limited by the accessibility of larger data sets for non-listed companies. We hope that the increasing number of companies listed on the Stock Exchanges and reporting more information on corporate governance will also help to expand the scope of research in this area.

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