

CORPORATE GOVERNANCE ON FINANCIAL PERFORMANCE OF INSURANCE INDUSTRY

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Abstract

The role of corporate governance in financial institutions differs from that of non-financial institutions for the discretionary power of the board of directors would be limited especially in regulated financial systems where financial institutions are obliged to function through legislative and prescriptive procedures, policies, rules and regulations. This study, therefore, was aimed at examining the impact of corporate governance on the performance of closely regulated Ethiopian insurance Industry. The study employed explanatory research design with an econometric panel data of 10 Insurance companies that covers the period 2007 to 2014. Board size, board independence and board diversity have negative and insignificant effect on the performance of insurance companies while size and independence of audit committee and frequency of board meetings have positive but insignificant effect on the performance of insurance companies in Ethiopia. Thus it could be concluded that all corporate governance mechanisms have insignificant effect on the performance of insurance companies measured by return on asset. This vividly affirms that the role of board of directors in closely regulated financial sector is dismal and insignificant for they have limited discretionary power to exercise as board of directors. Thus it would be recommendable if the regulatory body could relax its prescriptive and stringent policies and devolve its power to board of directors without endangering the viability of insurance companies.

Keywords: Corporate Governance, Insurance Companies, Board of Directors, Ethiopia

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1. Introduction

Corporate governance can be defined as the relationship among shareholders, board of directors, top management, employees, regulators, any other stakeholders and the community in determining the direction and performance of the corporation (Ruin, 2001). The boards of directors have an important role in alleviating the agency costs that arise from the separation of ownership and decision control in corporations (Fama and Jensen, 1983). Short et al. (1999) also took this view and argued that the boards of directors are the central corporate governance control mechanism responsible for monitoring the activities of managers, whilst Jensen (1993) describes the board of directors as the apex of the internal control mechanism in an organization. Therefore, the sole existence of board of directors is to protect the interests of shareholders from where it receives its authority for internal control (Jensen, 1993).

Firms with better corporate governance mechanisms continue to attain organizational objectives and goals than those that do not have (Bradley (2004). Adams and Mehran (2003), argues

that organizations with better systems and procedures are important for firms' performance. Better policies and procedures have been recognized as a significant factor in improving financial performance of organizations. Many authors argues that if an organization pays attention in having and following systems, then it will be in position to generate better returns to its shareholders (Matama, 2005; Gompers et al. (2003). Corporate Governance is aimed at ensuring proper governance of business as well as complying with all the governance norms prescribed by regulatory body for the benefit of all interested parties including society. The board of directors has an important role in alleviating the agency costs that arise from the separation of ownership and decision control in corporations (Cheung and Chan, 2004).

Studies also show that corporate governance in financial institutions differs from that in the non-financial institutions because of the broader risk that financial firms pose to the economy. As a result the regulator plays a more active role in establishing standards and rules to make management practices in financial institutions more accountable and efficient and hence financial sector regulators place additional

responsibilities on board of directors' that often result in detailed regulations regarding their decision-making practices and strategic aims. These additional regulatory responsibilities for management have led some experts to observe that banking regulation is a substitute for corporate governance (Renee and Hamid, 2003).

The apex regulatory body is more active than the board of directors of financial institutions in devising governance standards, promoting the interests of shareholders, depositors and other stakeholders. Thus the role played by directors of financial institutions would not be at par with non-financial institutions. Corporate governance matters are governed and driven by countries' company's codes, securities and exchange commissions, the stock exchange listing requirements, regulations and rules and other country specific regulatory agencies (Anthony, 2007).

In Ethiopia where the financial sector is closed and subject to stringent regulatory system, exploring impact of corporate governance mechanisms on the performance of insurance industries is quite interesting. The extant literatures explain only the effect of corporate governance on the performance of firms (Matama, 2005; Joan, et.al, 2010; Rashid, 2011; David and Tobias 2013). These studies attempted to explain the effect of corporate governance on the performance firms in relatively liberalized economy where the board of directors has more discretionary power to exercise their power and to make decisions that they felt are more worthy to their firms.

This paper argues that board of directors have limited role to play in Ethiopian insurance companies, where they are obliged to implement legalistic and prescriptive policies, procedures, rules and regulations set by the regulatory body, National Bank of Ethiopia. The regulatory body prohibits foreign entry into the industry, regulates capital requirements, imposes ownership limitations, restricts types of business and investment insurance companies could engage and the amount of investment they could make, remuneration and appointment of executives and inter alia.

This study aims to explain the role of board of directors on stringently regulated insurance industry in Ethiopia and would contribute its part in explaining the role of corporate governance mechanisms in the absence of capital markets in closed Ethiopian Financial sector. The rest of the paper is organized as follows. Section 2 presents review of related literature. Section 3 describes the research designs and methodology. Section 4 deals with results and discussion. Section 5 presents the conclusion and policy implications of the findings.

2. Literature Review

2.1 Review of Theoretical Literature

There are various theories that can be used to explain corporate governance conventions and also the issues that arise as a result of these conventions (Rashid, 2011). These theories include the agency theory, stakeholder theory, stewardship theory and resource dependency theory (Sanda and Garba, 2005; David and Tobias 2013). These four theories as the main and most significant theories of corporate governance are explained further respectively below.

2.1.1 Agency Theory

The essence of this theory is based on the existence of separation between ownership and management of corporations. In such corporations, the managers (agents) are hired to work and make decision on behalf of the owners (principals) in order to maximize return to the shareholders. However, the managers (agent) who are put in control of the affairs of the organization may not always consider the best interest of the owners and may pursue their self-activities to the detriment of the welfare of the principals (David and Tobias 2013).

As a result of these agency problems, the principal might end up incurring costs known as Agency costs. This Agency cost is a value loss to the shareholders and usually involves the cost of monitoring the activities of managers so that goal congruence can be achieved between shareholders and managers. The effect of this agency theory is that one can only try to mitigate against this agency problem when the board is composed largely by non-executive directors (independent and dependent) who will be able to control the activities of managers and thereby maximize shareholders' wealth. The governance structures suggested by the agency theory involve size of the board, composition of the board, remuneration to CEO, directors' shareholding and shareholder right (Luan & Tang, 2007; Rashid, 2011).

The theory also suggests that the role of the chairman and the role of the CEO should not be occupied by the same person as this can limit the monitory role bestowed on the board of directors and can also have a negative impact on the performance of the firm. It was suggested that the reason for limit in the monitory role by the board will be loss of board independence as a result of CEO duality (Elsayed, 2007 and Kang & Zardkoohi, 2005). This theory is based on the belief that there is a basic conflict of interest between the owners and managers of the company (Kiel & Nicholson, 2003).

2.1.2 Stewardship theory

A steward is defined by Davis, Schoorman & Donaldson (1997) as one who protects and maximizes

shareholders wealth through firm performance, because by so doing, the steward's utility functions are maximized. In this perspective, stewards are company executives and managers working for the shareholders, protects and make profits for the shareholder (cited in David and Tobias 2013). This theory is a contrast or a direct opposite to the agency theory and this theory adopts a more idealistic view of humans. This theory is based on a belief that the agent is not self-opportunist but a steward that perceives greater utility in the interest of the principal and the organization as a whole. The theory assumes that a significant correlation exist between the firm's success and the manager's satisfaction. This trade-off is achieved by the steward admitting that working towards achieving company's and collective goals will lead to self actualization. The theory argues for the post of Chief Executive Officer and Chairman to be held by the same person. Therefore, control lowers the motivation of steward and weakens motivational attitude (Davis et al., 1997).

Stewardship theory poses that stewards are likely to ignore selfish interests in order to pursue the best interest of the firm. Davis et al, (Ibid) observed that when a steward has been in a company for so long, the steward and the firm becomes one entity. Instead of using the firm for their own selfish interest, the stewards seems to be more in ensuring the continuous existence and long term success of the firm because they now see the firm as an extension of themselves (David and Tobias 2013).

2.1.3 Stakeholder theory

The other popular theory of corporate governance is the Stakeholder theory. The stakeholder theory originated from the management discipline and gradually developed to include corporate accountability to a broad range of stakeholders (Abdullah and Valentine, 2009). Unlike the agency theory, whereby managers are predominantly responsible for satisfying the interests of shareholders, stakeholder theory maintains that managers in organizations are not only responsible for the interests of shareholders but also for a network of relationships to serve which includes the suppliers employees and business partners (Ibid).

According to stakeholder theory decisions made regarding the company affect and affected by different parties in addition to stockholders of the company. Hence, the managers should on the one hand manage the company to benefit its stakeholders in order to ensure their rights and their participation in decision making and on the other hand the management must act as the stockholder's agent to ensure the survival of the firm to safeguard the long term stakes of each group (Fontain et al., 2006).

2.1.4 Resource Dependency Theory

Resource dependency theory concentrates on the role of board directors in providing access to resources needed by the firm while the stakeholder theory focuses on relationships with many groups for individual benefits. Hillman et al. (2000) contend that resource dependency theory focuses on the role that directors play in providing or securing essential resources to an organization through their linkages to the external environment. Indeed, Johnson et al, (1996) concurs that resource dependency theorists provide focus on the appointment of representatives of independent organizations as a means for gaining access in resources critical to firm success. It has been argued that the provision of resources enhances organizational functioning, firm's performance and its survival (Daily et al, 2003).

2.2 Empirical literature

There are scanty and inconclusive studies and findings on the effect of corporate governance mechanism on the financial performance of Insurance companies in developing countries (Joan, et.al, 2010).

In many of empirical studies corporate governance mechanisms had been dealt and categorized as endogenous and exogenous governance mechanisms. Endogenous corporate governance mechanisms are otherwise known as internal corporate governance. Internal corporate governance is about mechanisms for the accountability, monitoring, and control of a firm's management with respect to the use of resources and risk taking this starts with the board of directors which is the supreme governing body of insurance company. Exogenous corporate governance mechanisms are external governance mechanisms related external force and regulation with the power to discipline the agent (Joan, et.al, 2010; Sapovadia, 2009).

Many researchers argued that the board of directors is the central corporate governance control mechanism responsible for monitoring the activities of managers and improving the performance of firms and board of directors have been described as the apex of the internal control mechanism in an organization (Jensen (1993; Hillman et al. 2000; Joan, et.al, 2010).

It is constantly debated what the right mix of governance structure (size of the board, composition of the board and frequency of board meetings should be and how a company performs is dependent on these governance structures (Das and Gosh, 2004). Al-Hawary, S (2011) Investigated the effect of governance mechanisms such as board size, CEO duality, percentage of non-executive directors, capital adequacy, the ownership percentage of large shareholders, and the ownership percentage of the largest shareholders of Jordanian commercial banks as measured by Tobin's Q and found that CEO duality, and percentage of nonexecutive directors had

statistically significant positive effect on performance; whereas leverage had statistically significant negative effect on performance. With regard to CEO-Chairman duality, National bank of Ethiopia has already prohibited the duality of the CEO in contrary to what is common in the boards of some firms in some countries that allow the CEO to be a board chairman. This CEO-Chairman split in the Ethiopian case is a positive move towards more independent boards to discharge their oversight and monitoring role and this variable could not be an issue for consideration. The empirical review of the literature has focused on more relevant explanatory variables that are deemed to have effect on the performance of Ethiopian Insurance companies. These endogenous explanatory variables considered in this paper include board size, board independence, size and independence of audit committee, board diversity and frequent of board meeting.

Board size is defined as the number of directors on the board. There is a view that larger boards are better for firm value because they have a range of expertise to help make better decisions, and are harder for a powerful CEO to dominate. Dallas, G (2004), states that the size of the board has positive effect and is an important governance consideration. However, some authors have advocated for smaller boards. Fama & Jensen (1983) argue that large boards are less effective and are easier for the CEO to control.

When a board gets too big, it becomes difficult to coordinate, encourages free riding and poses problems. Smaller boards however reduce the possibility of free riding, and increase the accountability of individual directors. Hence there will be a positive or negative relationship between board size and firm value.

Adetunji and Olawoye (2009) argue that board size determines the number of directors in a board and the board should be of reasonable size, and the terms of its directors should be fixed and advocates for optimal size of board of directors for good corporate governance as well as performance in the firm. Of course the National bank of Ethiopia (2014) has stated the minimum number of board size of an insurer to be nine. The question "what would be the optimum board size remains debatable and inconclusive (Houssein and Ines, 2011; Ishaya, Francis and Solomon, 2013; Adeusi et al., 2013; Musa et al., 2013; Turku, 2014; Anthony, 2007). The aforementioned empirical review of the literature leads to develop the hypothesis that board size has positive and significant effect on the performance of insurance company.

Board independence: sometimes called board composition is measured as the ratio of independent (external) board members to the total number of board members. There are empirical evidences supporting that the higher proportion of outsiders on a board can better monitor and control the opportunistic behavior of the incumbent management, thus, minimizing the agency problem and maximizing shareholders' wealth

(Martin and Sebastian, 2011; Anthony, 2007; Cassandra et al., 2009; Lorne and Jun, 2012; Adeusi et al., 2013; Musa et al., 2013). Of course negative association between board composition and firm performance was reported by Agrawal and Knoeber (1996), who find that more outsiders on the board negatively affect the performance and conclude that outsiders are added on boards for political reasons and they reduce performance directly or by proxy for the underlying political constraints that led to their board memberships. With such inconclusive findings in this study it has been hypothesized as the board independence has positive and significant effect on financial performance of insurance company

Audited Committee size and independence: Review of the literature has revealed that existence of independent and competent audit committees has positive effect on firm performance (Anthony, 2007; Cassandra et al., 2009). Audit committee help to ensure that accounting policies are sound and financial statements are properly prepared and audited. Moreover, the existence of audit committee composed of external board members in the firm will create a transparent and credible environment between management, external auditors and the board members.

The evidence suggests that existence of audit committee improves governance quality and financial performance of firms (Defond, et al., (2005; Green, 2005). Thus it has been the hypothesized as there is positive relationship between independent audit committee and financial performance of insurance company.

Board diversity: In recent years, there has been an increasing interest in investigating the impact of gender diversity on the firm's performance, which is whether the addition of women to the board affects performance, and a number of research projects have attempted to provide evidence for this argument. The empirical study by Smith et al., 2005; Huse, 2007 and Mersland and Strom, 2007) have found that the presence of women in the board positions have a positive effect on the firm's performance. Thus it could be hypothesized as board diversity has positive effect on the financial performance of insurance company.

Frequency of board meetings: frequency of board meeting as corporate governance are considered as important proxies for the time directors spend monitoring managerial performance and also as an important resource in improving the effectiveness of a board (Funmi, 2014). When boards hold regular meetings, they are more likely to remain informed and knowledgeable about relevant performance of the company leading them to take or influence and direct the appropriate action to address the issue (Adams, 2000; Abbott et al., 2003; Funmi, 2014). Indeed Jensen (1993) found negative relationship and suggests that board meetings were a reactive response and not a proactive measure.

The negative association between frequency of board meeting and performance was further confirmed by Vafeas (1999) and Karamanou and Vafeas (2005). National bank of Ethiopia (2014) stated the board shall set up and put in use rules for the manner of conducting board meetings and Board meetings shall be held at least once in a month. Keeping in view of these empirical literatures and regulatory requirement, frequency of board meeting has positive and significant effect on financial performance of insurance company.

3. Research Methodology and Model specification

3.1 Sample Selection

According to the data gathered from the National Bank of Ethiopian website the numbers of insurance companies operating in the market at the end of June 2014 were 16 in numbers. Of these 6 insurance companies were established since 2010 and are in operation for few years. Thus purposively, 10 of the insurance companies were included in the sample for analysis.

3.2 Source of Data

Data for this study is secondary data obtained from audited annual financial statements of the respective insurance companies and from the website of National bank of Ethiopia. The study included 10 Insurance companies. The study used panel data of 10 Insurance companies that covers the period 2007 to 2014 (10 years) (80 observations).

3.3 Selection of the variables

Corporate governance mechanisms such as board size, board independence, Audit committee size and independence, frequent of board meeting, board diversity were selected as endogenous independent variables in the study. Age and size of the insurance companies were also incorporated as control variables. ROA was considered as dependent variables.

3.4 Econometric Model specification

A quantitative method of data analysis was employed which involved descriptive and inferential statistical analysis. The descriptive statistics were used to analyze the means and standard deviations of regression variables. The assumptions and tests of Classical Linear Regression Model (CLRM) were tested before conducting regression analysis. The following regression model was used to explain the effect of corporate governance mechanisms on financial performance of insurance company:

$$ROA_{it} = \alpha_0 + \alpha_1 BSIZE + \alpha_2 BIND + \alpha_3 ACSIZE + \alpha_4 ACIN + \alpha_5 BDIV + \alpha_6 FBM + \alpha_7 FSIZ + \alpha_8 FAGE + E$$

Where:

α_0 = Intercept

ROA = Dependent variable, Return on Asset

BFSIZE = Board size representing the number of directors sitting in the board

BIND = the percentage of external board members to the total number of board members

ACSIZE = Number of Audit committee members

ACIN = percentage of independent audit committee members to total audit committee members

BDIV: Board diversity, Percentage/proportion of women in the board

FBM = Frequency of board meetings (number of board meetings per year)

FSIZ = Firm Size as natural logarithm of total assets of an insurance company

FAGE = Age of the insurance company in years

3.5 Diagnostic Test for the Regression Assumptions

Diagnostic test were conducted by using STATA version 12. The goodness of fitness of the model was tested through ANOVA and F-statistic and was proven that the explanatory variables used in the model actually explain the variations in the dependent variable (ROA). The correlation matrix, Variance Inflation Factor (VIF) and Tolerance values shows that there is not multicollinearity among the explanatory variables. Normality and heteroscedasticity tests also portrayed that the normality, homoscedasticity assumptions of the regression model were satisfied to run the regression analysis.

Finally, to select a best fitted model between the alternatives of random effect model and fixed effect model, Hausman test was conducted. The p-value of Hausman test is 0.0358 which is less than the level of significance (0.05). Therefore, the null hypothesis which claims the unique errors (U_i) are not correlated with the regressors was rejected and fixed effects become more appropriate than Random effect. Further test was also conducted to choose between fixed effects versus pooled OLS regression model by using Breush and pagan Lagrangian multiplier test and the result shows that Fixed effect is fitted for the study since the P-value is 0.0004 which is less than the significant level (0.05). Therefore, our suitable model could be fixed effect model.

4 Analyses and Interpretation of Results

Descriptive, correlation and regression analysis and interpretation of the results were made hereunder.

4.1 Descriptive statistics

Table 1 reports the descriptive statistics of the dependent and independent variables for the panel period from 2007 to 2014. The table presents the

mean, minimum, maximum and standard deviation for the panel data variables for the period from 2007 – 2014.

Table 1. Descriptive Statistics

Variables	Obs	Mean	Std. Dev.	Min	Max
ROA	80	0.077	0.04	-0.01	0.18
BSIZE	80	9.6	1.59	7	16
BIND	80	0.74	0.14	.42	0.89
ACSIZE	80	3.4	0.49	0	4
ACIN	80	0.65	0.19	0	0.75
BDIV	80	0.13	0.23	0	0.20
FBM	80	15.6	2.7	11	21
FSIZE	80	19.11	1.04	16.9	21.2
FAGE	80	15.6	8.0	1	39

Source: Author's computation

For the ten insurance companies included in this study, the average return on asset (ROA) was 7.7% while the minimum and maximum return being negative 1% and 18%, respectively with standard deviation of 4%. The average size of the board was nearly 10 with minimum size of 7 and maximum of 16 board members with significant standard deviation of 159%. With regard to board independence on the average 74% of the board members are external with minimum and maximum percentage of 42% and 89%, respectively, implying that board of directors are relatively independent as they are mostly dominated by non executive directors.

The average size of audit committee members was nearly 3 with minimum size of 0 and maximum of 4 audit committee members. The average percentage of independent audit committee members were 65% with minimum and maximum of 0 and 75%, respectively. The minimum audit committee size of zero and Audit committee independence of zero implies that in some of the insurance companies audit committee was not established during that specific observation period.

With regard to board diversity, on the average only 13% of the board members are composed of

female directors with minimum of 0 and 20%, implying that there are insurance companies whose boards of directors are 100% composed of males. The average number of board meetings was nearly 16 times per year while the minimum and maximum numbers of board meetings were held for 11 and 21 times per year. The size of the sampled insurance companies, taken as the logarithmic of total asset, indicated a mean value of 19.11, and a minimum and a maximum value of nearly 17 and 21, respectively. The average age of the insurance companies were nearly 16 years with minimum and maximum of 1 and 39 years. This shows that except the state owned Ethiopian insurance company, all private insurance companies were established following deregulation of the financial sector since 1994.

4.2 Correlation matrix

Table-2 shows the summary of correlation coefficient between dependent variables (ROA) and explanatory variables. From the table it was observed that multicollinearity was not a threat to the model variables.

Table 2. Correlation matrix

---	ROA	BSIZE	BIND	ACSIZE	ACIN	BDIV	FBM	FSIZE	FAGE
ROA	1.0000								
BSIZE	0.1188	1.0000							
BIND	0.0327	-0.6005	1.0000						
ACSIZE	-0.1447	0.1487	0.1097	1.0000					
ACIN	-0.0105	0.2135	0.1217	0.4234	1.0000				
BDIV	-0.1129	-0.1074	0.2026	0.1585	0.1409	1.0000			
FBM	0.4120	-0.1864	0.0739	-0.0249	-0.0768	0.0222	1.0000		
FSIZE	0.4643	0.1362	0.0747	-0.0573	-0.0108	0.1239	0.4756	1.0000	
FAGE	0.4201	-0.0131	0.1575	-0.0199	-0.0341	0.0182	0.5115	0.7342	1.0000

Source: Author's computation

As portrayed in table-2, board size, frequency of board meetings, firm size and age have positive correlation with the performances of the insurance companies. However independence of the board, size of audit committee and its independence and board diversity have negative relationship with the profitability of the insurance companies. The correlation matrix also revealed the relationship between explanatory variables. The correlation matrix has also indicated that the multicollinearity is not a threat to the model variables as all correlation coefficients are below the threshold level of 0.8 (Gujarati, 2004).

4.3 The Regression Analysis and Interpretation

The regression analysis in Table-3 shows the impact of corporate governance mechanisms on the performance of Ethiopian insurance companies. As it has been already discussed in the research methodology fixed effect model was found fit for panel data analysis and therefore, our empirical analysis were based on fixed effect model. The p-value of "F" was 0.0053, which is less than 5% and confirms that the model is appropriate to explain the panel data.

Table 3. Regression Analysis

Fixed-effects (within) regression		Number of obs = 80				
Group variable: FIRM		Number of groups = 10				
R-sq: within = 0.2853		Obs per group: min = 8				
between = 0.2905		avg = 8.0				
overall = 0.1986		max = 8				
corr(u_i, Xb) = -0.8782		F(8,62) = 3.09				
Prob > F = 0.0053						
ROA	Coef.	Std. Err.	T	P> t	[95% Conf. Interval]	
BSIZE	-.0042949	.006302	-0.68	0.498	-.0168924	.0083025
BIND	-.0816083	.0804827	-1.01	0.315	-.0168924	.0792744
ACSIZE	.0035088	.0101678	0.35	0.731	-.0168164	.023834
ACIN	.0055516	.0265773	-0.21	0.835	-.0586788	.0475757
BDIV	-.0159456	.0175904	-0.91	0.368	-.0511083	.0192172
FBM	.0032748	.0028332	1.16	0.252	-.0023886	.0089382
FSIZE	.0009031	.0117126	0.08	0.939	-.02251	.0243163
FAGE	.0082839	.0031139	2.66	0.010	.0020594	.0145085
_cons	-.0256501	.206894	-0.12	0.902	-.4392254	.3879251
sigma_u	.06127165					
sigma_e	.03153539					
Rho	.79057815 (fraction of variance due to u_i)					
F- test that all u_i=0:			F(9, 62) = 4.85	Prob > F = 0.0001		

Source: Author's computation

The empirical result of the study under fixed effect estimation technique shows that board size has negative and insignificant effect on the performance of the insurance companies leading to the rejection of research hypothesis. Though insignificant this finding was consistent with findings of (Fama & Jensen, 1983; Adetunji and Olawoye, 2009) who advocate that large board size has adverse effect on the performance of firms but contradict with findings of Dallas, G (2004) who states that the size of the board has positive effect on performance of firms. Unless the type and nature of the industry and the discretionary power of board of directors is considered the optimum size board size remains debatable and inconclusive as claimed by Houssein and Ines, 2011; Adeusi et al., 2013; Musa et al., 2013 and Turku, 2014).

The empirical study would dare to prove that in repressed and regulated financial sector the boards of directors have limited power and its size doesn't matter as decisions are made within prescribed policies and rules of regulatory body. Board independence which is measured as the ratio of external board

members to the total number of board members has negative and insignificant effect on the performance of insurance companies proving for rejection of research hypothesis. This finding is supported with the previous empirical finding of Agrawal and Knoeber (1996) who found negative association between board independence and firm performance. This finding, of course, contradicts the findings of Anthony, 2007; Cassandra et al., 2009; Lorne and Jun, 2012; Adeusi et al., 2013; Musa et al., 2013) who reported positive association between board independence and firm performance. Despite the fact that on average 75% of board members are composed of independent board members (Table-1), the negative association between their independence and firm performance shows that board of directors have limited power to exercise as board of directors.

Interestingly size of audit committee and audit committee independence has positive but insignificant effect on the performances of insurance companies. This finding compliments with (Green, 2005); Anthony, 2007 and Cassandra et al., 2009), who

revealed the positive effect of independent and competent audit committees on the performances of firms.

Board diversity measured by the presence of women in the board has negative effect on the firm's performance. This finding contradicts with (Smith et al., 2005; Huse, 2007 and Mersland and Strom, 2007) who have found that the presence of women in the board positions have a positive effect on the firm's performance. This would not come as surprise as board size itself has negative effect on the performances of insurance companies. Frequency of board meetings which is considered as an important proxies for the time directors spend monitoring managerial performance has positive but insignificant effect on the performances of insurance companies. This is consistent with studies of (Adams, 2000; Abbott et al., 2003; Funmi, 2014). Indeed it contradicts with (Jensen (1993 Karamanou and Vafeas, 2005) who reported negative relationship between number of meetings and firm performances.

The control variables firm size and firm age have got positive relationship with the performances of the insurance companies. In a nutshell, board size, board independence and board diversity have negative and insignificant effect on the performance of insurance companies in Ethiopia. However, Size and independence of audit committee and frequency of board meetings have positive but insignificant effect on the performance of insurance companies in Ethiopia. The study in general found that all corporate governance mechanisms considered for investigation have insignificant effect on the performances of insurance companies implying that under stringently regulated financial industry board of directors have limited discretionary power and regulatory body has much more influential power than the board of directors.

Conclusions and Recommendations

The effect of corporate governance on firm performance has been such a buzz research topic that has attracted the attention of both academicians and researchers. Though there are extant empirical literatures, the outcome of such empirical studies has remained inconclusive. Few studies have shown that corporate governance in financial institutions differs from that of non- financial institutions and hence the discretionary power of the directors would be limited especially in regulated financial systems, where financial institutions are obliged to function through legislative and prescriptive procedures, policies, rules and regulations. This study, therefore, aims at examining the impact of corporate governance on the performance of closely regulated Ethiopian insurance Industry.

Eight years panel data from ten insurance companies were employed and analyzed through fixed effect model. The return on assets of the sampled

insurance companies on average was 7.7% with average board size of nearly 10 board members. Of the total board members, 75% of them were non executive board members that in turn have paved the way for establishing an audit committee that is composed of independent board members. Almost 90% of the board members were composed of males and on average board of directors have held 16 meetings per year.

Board size, board independence and board diversity have negative and insignificant effect on the performance of insurance companies while size and independence of audit committee and frequency of board meetings have positive but insignificant effect on the performance of insurance companies in Ethiopia. Thus it could be concluded that all corporate governance mechanisms have insignificant effect on the performance of insurance companies measured by return on asset. This vividly affirms that the role of board of directors in closely regulated financial sector is dismal and insignificant for they have limited discretionary power to exercise as board of directors. Thus it would be recommendable if the regulatory body could relax its prescriptive and stringent policies and devolve its power to board of directors without endangering the viability of insurance companies.

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