THE IMPACT OF CORPORATE GOVERNANCE ON PROFITABILITY OF NEPALESE COMMERCIAL BANKS

A Thesis

Submitted by:

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Exam Roll No.: 5329
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Submitted to:

OFFICE OF THE DEAN
FACULTY OF THE MANAGEMENT
TRIBHUVAN UNIVERSITY

In partial fulfillment of the requirements of the degree of Master of Business Studies (MBS)

New Baneshwor
Kathmandu
April, 2013

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RECOMMENDATION

This is to certify that the thesis

Submitted by

Tirtha Laxmi Manandhar

Entitled

THE IMPACT OF CORPORATE GOVERNANCE ON PROFITABILITY OF NEPALESE COMMERCIAL BANKS

has been prepared as approved by this department in the prescribed format of Faculty of Management. This thesis is forwarded for examination.

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Mr. Rabindra Kumar Neupane	**Dr. Sushil Bhakta Mathema**
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VIVA-VOCE SHEET

We have conducted the viva-voce examination of the thesis of presented by

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and found the thesis to be the original work of the student and written according to the prescribed format. We recommend the thesis to be accepted as partial fulfillment of the requirements for

Master's Degree in Business Studies (M.B.S.)

VIVA-VOCE COMMITTEE

Head of Research Department : ……

Member (Thesis Supervisor) : ……..

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Member (External Expert) : ……

DECLARATION

I hereby declare that the work reported in this thesis entitled **The Impact of Corporate Governance on Profitability of Nepalese Commercial Banks** submitted to Nepal Commerce Campus, Faculty of Management, Tribhuvan University is my original work done in the form of partial fulfillment of the requirement of the degree of Master in Business Studies (M.B.S) prepared under the supervision of Dr. Sushil Bhakta Mathema and Mr. Rabindra K. Neupane, Nepal Commerce Campus.

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It is very complicated to prepare this thesis being student of MBS. I could not prepare this thesis without taking help of many individuals. So, I would like to thank all of the individuals who help me to prepare this thesis.

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BM: Board Meeting

CG: Corporate Governance

GDP: Gross Domestic Product

NPL: Non Performing Loan

NPR: Nepalese Currency

NRB: Nepal Rastra Bank

OECD: Organization of Economic Co-operation and Development

ROA: Return on Assets

ROE: Return on Equity

SCOS: Size of Board of Directors

SHOD: Number of Shareholders

1.1 General Background

Corporate governance is the set of processes, customs, policies, laws, and institutions affecting the way a corporation (or company) is directed, administered or controlled. Corporate governance comprises the long-term management and oversight of the company in accordance with the principles of responsibility and transparency (OECD, 2010).

Corporate governance is a key element in improving economic efficiency, which involves a set of relationships between a company's management, its board, its shareholders and other stakeholders. It also provides the structure through which the objectives of the company are set and the means of attaining those objectives and monitoring performance are determined. Corporate governance is a term that refers broadly to the rules, processes, or laws by which businesses are operated, regulated, and controlled. The term can refer to internal factors defined by the officers, stockholders or constitution of a corporation, as well as to external forces such as consumer groups, clients, and government regulations. Well-defined and enforced corporate governance provides a structure that, at least in theory, works for the benefit of everyone concerned by ensuring that the enterprise adheres to accepted ethical standards and best practices as well as to formal laws. To that end, organizations have been formed at the regional, national, and global levels.

Corporate governance has been an issue of global concern long before now. However, it came to the fore in the 1980's as fallout of the Cadbury report in the United Kingdom, which concentrated on the financial aspects of corporate governance. Immediately following suits, the subject of corporate governance reverberated round developed and developing countries. The Governance of banks becomes even more pronounced considering their role of financial intermediation in developing economies. Commercial banks are the main providers of funds to enterprise and where there is a thin or absent capital market, their failure becomes the failure of the system. The fundamental issue of corporate governance and banks performance cannot be complete without proper understanding of the functions of shareholders and directors; the creation

of an efficient and reliable board from among the shareholders to checkmate director's excesses if any becomes a sine qua non. This is so because even in some instances, the corporations whose turnover are larger than the GDP of some developing countries. It becomes pertinent to ask if there is a link between corporate governance and performance.

Sound corporate governance is an important element of sustainable private sector development - not only because it strengthens businesses' ability to attract investment and grow, but also because it makes them, stronger, more efficient, and more accountable. The definition of corporate governance most widely used is "the system by which companies are directed and controlled". Corporate governance has been the buzzword in Nepal in recent years. Nepal Rastra Bank (NRB) has issued directives on good corporate governance. It is a clear indication of central bank's commitment to bring about high level of corporate governance. With the advent of economic liberalization and public limited companies being listed in the stock exchange, a felt need for better corporate practices has emerged. Good corporate governance is not an old concept for the Nepalese financial system. Prior to the open licensing system for the establishment of Bank and Financial Institution, authorities were not found so concerned about good governance of financial institutions. The absence or the denial of good governance led two old public sector commercial banks Rastriya Banijya Bank and Nepal Bank Limited towards serious shortfall in all aspects of their governance. As soon as the new private and joint venture commercial banks and other financial institutions started their establishment in Nepal, the concerned Nepalese authorities started thinking seriously about the necessity of good corporate governance. Due to lack of accountability, lack of experience as well as expertise and the practice to use the facility in one's own interest it was observed that some of the banks and financial institutions were not following the principle of good corporate governance. Such practice seriously affected their profitability resulting in piling up of the non-performing assets. Nepal Rastra Bank as a custodian to Nepalese financial system came forward and started issuing relevant prudential regulations, which was the demand of the hour. Issuance of such regulations had been welcomed as a step towards restoring good governance in the banks and financial institutions. Regulation was aimed at helping them to enhance their deteriorated good governance conditions, which was thought as the root cause of non-performance.

To study about the corporate governance and its effect on the Profitability of Banks in Nepal, an article on "Does Corporate Governance affect Bank

Profitability? Evidence from Nigeria" by Akpan, Emmanuel S and Riman, Hodo B is taken as a base. For the study purpose, the data will be collected from the financial report of the selected banks.

In simple form, the corporate governance includes the interrelated and interlocked relation of the players like shareholders, the management, the board of directors, all the stakeholders including the society and the Government of the Nation. Academician treats it as a problem of separation of management and ownership and so on. The banks play a crucial role in building the economy and Nepal is no exception. Effective corporate governance in banks and financial institutions helps foster financial stability, strengthen risk management and ultimately contribute to a strong financial system. A sustainable growth in the economy is critically dependent on a sound financial system. Nepal is in a critical stage of transition. The fundamental issue of corporate governance and banks performance cannot be complete without proper understanding of the functions of shareholders and directors; the creation of an efficient and reliable board from among the shareholders to checkmate director's excesses if any becomes a sine qua non. This is so because even in some instances, we see corporations whose turnover are larger than the GDP of some developing countries. It becomes pertinent to ask if there is a link between corporate governance and performance.

1.2 Statement of the problem

After many corporate collapses of Enron, WorldCom, HIH Insurance because of poor governance and due to threatening of financial crisis is growing faster today; corporate governance structure has been put into focus and gets more concerns. Besides, the financial crisis of 1997 in East Asia countries has brought the need for CG's progress as an emergent demand.

Profit efficiency studies found that mergers and acquisition improve profit, which comes as a result of portfolio shifts. (Akhavein, Berger and Humphery,

1997). In considering performance, the main question is always on credit availability and portfolio allocation, as well as efficiency. This is because the objectives of states owned banks in particular centers on developing specific industries or region, export expansion and always engaged in directed lending. Studies for individual nations particularly with respect of changing fro state ownership to foreign ownership. Metico(Haber, 2005), Nigeria (Beck, Cull and Jerome, 2005), Brazil (Beck, Crivelli and Summerhill, 2005). Spon and Sullivan (2007) examine the relationship between banks ownership and several governance aspects and found out that increasing ownership stakes for hired managers and boards improves banks performance. However, for banks to perform its intermediating functions, certain issues like their objectives for being in existence must be considered.

According to Lefort and Urzua (2008), boards of directors are central institution in the internal governance of a company. In addition to strategic direction, they provide a key monitoring function in dealing with agency problems in the firm (Lefort & Urzua, 2008). Due to the importance of board of directors, many studies have concentrated on finding good structure and composition of the board and check if it affects firm performance. In addition, boards of companies with high ownership concentration will tend to be mostly comprised of directors who represent the owner manager's interests, thus being unable to deal with the specific agency problem adequately (Lefort & Urzua, 2008).

Pathan, Skully, Wickramanayake (2008) show a statistically significant negative relation between Thai banks' board size and performances, while a statistically significant positive impact of the proportion of independent directors on the bank board and performance for 1999-2003. Pinteris (2002) documents a negative relationship between bank ownership concentration and bank performance in the Argentinean banking industry. Crespí, García-Cestona, and Salas (2004) found a negative relationship between performance and governance intervention for Spanish bank.

Begger, Hanweek and Humphery(1987), using US data found very little scale economies or diseconomies on account of static differences in performance between domestically owned banks and their foreign and state owned counterparts. Deniser and Strahan(1997), actually found possible revenue benefits for large banks than small banks in 1990's. Deyoung, Hunter and Udell(2004), found that large and small banks serve different groups of

customers, use different technologies and /or have different effects on competition

Yung (2009), using panel regression methods, confirm board size has a great impact on bank performance. While Love and Rachinsky (2009), using a sample of 107 banks in Russia and 50 banks in Ukraine found some significant, but economically unimportant relationship between governance and contemporaneous operating performance and a weaker link with subsequent performance.

Yaser Fallatah and Denise Dickins carried out a research about the "*Corporate governance and firm performance and value in Saudi Arabia*". The objective of the study was to investigate the relationship between corporate governance characteristics and firm performance and value of Saudi-listed firms using an index intended to capture the combined effect of firms' corporate governance characteristics The data were gathered from Saudi-listed firms from the years 2006 to 2009 using nine corporate governance characteristics. These governance characteristics are selected based on the findings of prior research subject to availability of data. This that corporate governance and firm performance (measured as return on assets) are unrelated, but corporate governance and firm value (measured as Tobin's Q and market value of equity) are positively related.

Khatab et-al, (2011), carried out a research about *"Corporate Governance and Firm Performance: A Case study of Karachi Stock Market*" and the objective of the study were to investigate the relationship between corporate governance and firm's performance of twenty firms listed at Karachi Stock Exchange. The main objective of the study was to find whether profitability ratios i.e., ROA and ROE affect the performance of the firm?The performance of corporate governance is analyzed through Tobin's Q, while performance of the firms is measured by return on assets (ROA) and return on equity (ROE). The data set is obtained from the annual reports for the year 2005-2009. The multiple regression models are applied to test the significance of corporate governance and firm profitability. The result shows that leverage and growth have a positive relationship with Tobin's Q, which confirms a significant effect in measuring performance of the firm.

Akpan, Emmanuel S and Riman, Hodo B (2012) carried out a research about the "Does Corporate Governance affect Bank Profitability? Evidence from Nigeria" and the objective of the study were to examine the relationship between corporate governance and banks profitability in Nigeria. The data were

obtained from the annual reports of 11 out of 24 banks (46%) operating in Nigeria.

Corporate governance is equally significance to all types of corporate institution. Furthermore it is very crucial and essential element for the banking system because bank and financial institutions depends on the Other Peoples Money (OPM). There may be a gap among major stakeholder like owners, depositors and management. Very limited people have a right to access in resources and decision. Due to the lack of transparency and adequate control mechanism, there may be the chance of vested interest and moral hazard problems. It is a universal fact that the higher degree of transparency contributes towards the maximizing shareholders value and ensuring the fairness to rest of the shareholders. Corporate governance also enhances performance of the corporation by motivating manager to maximize returns on investment, raising operational efficiencies and ensuring long- term productive growth. Nepal is a developing country and facing with the problem of political instability, low economic growth, and higher inflation. There is no any proper code of Corporate Governance prevailing in Nepal. Therefore the attempt has been done to show the relationship between the bank performance (i.e. Return on assets (ROA), Return on equity (ROE), Non-performing Loans (NPL)) and other related variables. But the study doesn't provide any specific link between bank performances with other variables.

Though there are above mentioned empirical evidences in the context of other countries, no such evidences exist in the context of Nepal. This study therefore deals with the following issues:

1. How can corporate governance affect the profitability of the bank?
2. What is the relationship between Board size and performance of the commercial banks of Nepal?
3. What is the relationship between shareholder size and performance of the commercial banks of Nepal?
4. Do this study bridges a gap in the literature and contributes to the understanding of corporate governance and performance of banks?
5. What is the impact of total assets on performance of the commercial banks of Nepal?
6. What is the impact of total equity on performance of the commercial banks of Nepal?

1.3 Objectives of the study

The general objective of this paper is to examine the relationship of different corporate governance variables on the profitability of the commercial banks in Nepal.

The specific objectives are:

1. To explore the relationship between corporate governance and profitability of banking sector.
2. To explore the relationship between corporate governance and banks performance in Nepal

3. To examine the various aspects of corporate governance affecting banks' performance and profitability that determines of board size and composition, shareholders, total assets and total equity.

1.4 Significance of the Study

The study of the impact of corporate governance plays a vital role in the managerial decision. Every organization has to analyze its financial performance in every step of its operation, promotion and expansion.

This study will help to understand the effects of corporate governance on the performance of commercial bank and will also try to show the relevant factors affecting the performance of the Nepalese commercial banks. It could also serve as the example for the new banks as how to manage their bank and its shareholders. Importance of the study conducted will be to the students, teachers, bankers, customers, employees of bank, government, practitioners in the field of accounting and finance etc.

1.5 Limitation of the Study

This study is highly dependent on the annual report of the selected banks. Almost information and data needed for this study are available in annual reports and financial statements, which are informed publicly. So, this study just concentrates on collecting and retrieving data from Nepalese commercial bank. Therefore, there are some limitations in this study which are:

- Only five year's data of the selected bank are used for the study (2007-2011)
- Study is fully based on the annual report provided by the banks. Thus there is the limitation of prevailing secondary data.
- This study is only limited to the commercial banks of Nepal
- Due to time constraint, not all the related areas were possible to cover in depth
- Lack of literature and the study about corporate governance in the perspective of Nepal.

1.6 Organization of the Study

The study is about the corporate governance and profitability of commercial Bank of Nepal. It will be organized into five chapters. The first chapter will be the introductory chapter which will provide information on the corporate governance practices in Nepal, statement of problem, and objectives of the study, formation of research hypotheses, significance and limitations of the study. The second chapter will be the review of literature. The third chapter will focus on the research methodology that will be applied to complete the study. The fourth chapter will be the presentation and analysis of data and the fifth chapter will be summary and conclusion of data.

As discussed before, CG is a set of international benchmark for application in a variety of countries. It is more than minimum compliance with laws and regulations but a way to encourage companies to improve their performance in international market. In this part, firstly I will introduce generally theory of CG Principles. Secondly, the role of board of directors and ownership concentration in line with the performance of companies will be explained. Then, literature review part summarize on relating researches in the past. Next, I consider and discuss the performance in adoption of CG in previous studies and the regulation of CG in Vietnam. Finally, theoretical framework between dependent variables and control variables will be shown up to refer for this study.

2.1 Introducing of Corporate Governance Principles

CG is concerned with the relationship between the internal governance mechanisms of corporations and society's conception of the scope of corporate accountability (Deakin and Hughes, 1997). In general, CG Principles covers following areas:

I) The rights of shareholders;

II) The equitable treatment of shareholders;

III) The role of stakeholders;

IV) Disclosure and transparency; and

V) The responsibilities of the board.

Each Principle is explained more details as following.

2.1.1 Rights of Shareholders

Based on the OECD Principles (OECD, 2004b), the CG framework should protect and facilitate the exercise of shareholders' rights. Shareholders should have rights to transfer shares, obtain relevant information of the company, participate and vote in general shareholders meetings, elect and remover members of the board decide on the remuneration of the board member or executives and get the dividend and share-repurchase (OECD, 2004). Besides, shareholders need to be noticed on decisions concerning fundamental corporate changes such as projects or investment information, rules concerned to voting

process for example. One important point in this principle is that does company have antitakeover defense to protect the rights of shareholders.

2.1.2 Equitable Treatment of Shareholders

Based on the OECD Principles (OECD, 2004), CG framework should ensure the equitable treatment for all shareholders, from majority shareholders to minority, from national to foreign shareholders (OECD, 2004b). All shareholders should have the opportunity to obtain effective redress for violation of their rights. Within any series of a class, all shareholders should be treated equally in voting, receiving the information, etc. Besides, minority shareholders should be protected from abusive actions and be able to influence board composition. OECD also prohibits insider trading and abusive self-dealing which influence to the treatment equally (OECD, 2004b).

2.1.3 The role of Stakeholders in Corporate Governance

Law or mutual agreements should describe clearly the rights and interests of stakeholders including employees, creditors, suppliers and so on. The companies not only assure the rights of stakeholder but also make the best condition for stakeholders to participate in the CG process. For instance, they should be able to access the relevant, sufficient and reliable information on time.

2.1.4 Disclosure and Transparency

Based on the OECD Principles (OECD, 2004), CG framework should ensure that timely and accurate disclosure of all material matters regarding the corporation, including the financial report, financial statement, annual report, majority share ownerships, remuneration of board member and key executives, selection process, related party transactions, information on the general shareholder meeting or managers' meeting and so on (OECD, 2004b). Besides, channels for disseminating information such as company's website, stock market's web, and press release of company, etc…should provide for equal, timely and easily access.

2.1.5 Responsibilities of the Board

The CG framework should ensure the strategic guidance of the company, the effective monitoring of management by the board, and the board's accountability to the company and the shareholders (OECD, 2004). Firstly, the board should apply high ethical standards, treat all shareholders fairly and have independent judgments on corporate affairs (OECD, 2004b). To do that, they should be able to access the relevant information if needed. Besides monitoring the effectiveness of the company's governance practices and making changes as needed, managing and solving the potential conflicts of interests between management, board members and shareholders are also the important duties of the board. In addition, in some cases, they can replace key executives and oversee their activities.

2.2 Literature Review

From the abundance of literature on corporate governance, much of it supports the idea that good corporate governance matters, and that it can affect both equity prices, as well as the capability for a firm to finance its operations and the cost of capital. Its importance arises in modern corporations due to the separation of management and ownership control in the organizations. The interests of shareholders are conflicting with the interests of managers. There are numerous studies on the ownership structure and the corporate governance and its impact on firm performance. Corporate governance is necessary ingredients for the firm performance as well as for the overall growth of the economy of the country. Most of these studies support the notion that there is a positive relationship between effective corporate governance (namely: number of shareholders, firm size and board size) and firm performance. Due to the vastness of topics on corporate governance this study has tried to focus only on literature directly related to our method of research, but I have also discuss any relevant topics as some of them are coherent in nature. Therefore, the following literature review must be looked upon as a guide on how the methodology is constructed.

Kapopoulos and Lazaretou (2007) used data of 175 greek listed firms in order to investigate whether there is strong evidence that ownership structure affects firm's performance, measured by profitability. Empirical findings indicate that there is a positive relationship between profitability and ownership structure in greek firms. Specifically, the results state that the greater the degree to which shares are concentrated in outside or inside shareholders, the more efficient the firm's management and as a result the firm's performance.

Love and Rachinsky (2008) in their paper investigate the connection between ownership, corporate governance and operating performance in the banking sector for the period 2003 – 2006. Yung (2009), using panel regression methods, confirm board size has a great impact on bank performance.

Pradhan and Adhikari (2009), carried a research about "*Corporate Governance and Firm Performance in Nepal*" and the objectives of the study were to analyze the corporate governance variables (such as institutional ownership, public directors and public capital) with firm performance and also examining the relationship of disclosure quality and firm performance. The major objective of this study is to examine the effect of fundamental variables on corporate governance in Nepal. This study used pooled cross-sectional data of 14 enterprises with 98 observations from 1997 to 2003. This study used Return on total capital employed, market price of share (MPS) as the variables that measure firm performance. The Leverage, institutional ownership to total ownership, public director to total director public capital to total capital and the Number of Shareholders (CBOD) measures the corporate governance index. The AGM conducted on time, financial statement submitted on time, A class auditor appointed as a dummy variables, while total Assets as control variables. These variables were examined by estimation of various econometric models. This study revealed the existence of the relationship between corporate governance practices and firm performance in Nepalese enterprises.

Akpan and Riman (2012) carried out a research about "*Does Corporate Governance affect Bank Profitability? Evidence from Nigeria*" and the objective of the study were to explain the relationship between corporate governance and banks performance in Nigeria from 2005 – 2008; considering the Soludo's consolidation (reform) agenda. The paper will also determine explicitly what variables explain corporate governance and how they impact on banks performance in Nigeria, within the period under review. The main objective of this study was to examine the relationship between corporate governance and banks profitability in Nigeria. This study used Return on Assets (ROA), Return

on Equity (ROE and Non-Performing loans (NPL) as the variables that measure bank performance. The number/size of Board of Directors (SBOD) and the Number of Shareholders (CBOD) measures the corporate governance index, while total Assets and Total Equity served as control variables applying the descriptive and correlation analysis to examine the relationship between Corporate Governance and Bank Performance in Nigeria. The result shows that good corporate governance and not assets value determine the profitability of banks in Nigeria. The study made four recommendations, one of which is to encourage banks to have small but qualitative board size that is made up of financial and legal professionals .

Corporate governance and firm performance

International agencies and domestic legal authorities have paid increasingly more attention to the review and reform of the company law following the Enron and Worldcom scandals in the US. According to Ma (2005), Hong Kong recently has established a clearly outline of responsible corporate governance arrangements.

The purpose of corporate governance is to coordinate a conflict of interests among all parties' relationship within the company and to develop a system that can reduce or eliminate the agency problems (OECD, 1997). It argues that the agency problems become more critical with weak governance and limited protection of minority shareholders in a company (Dharwadkar, George, & Brandes, 2000). OECD (1997) also outlines that sound corporate governance should be able to help the board of directors and managers to achieve the best interests of the company and shareholders.

Moreover, it can be argued that firm performance can be improved with better corporate governance controls in a company. Famma and Jensen (1983) argued that corporate governance does affect firm performance. They found that the majority of larger firms with stronger governance controls are rewarded over the long-term. Klein, Shapiro, and Young (2004) examined the relationship between corporate governance and firm value by using the Corporate Governance Index (CGI) and Tobin's Q, which measures the firm's value. The results conclude that corporate governance does matter in firm value.

In addition, Carse (2000) argued that a strong corporate governance standard is particularly important for banks. This is because most of funds that banks use for business belong to their creditors and depositors. The failure of a bank will affect not only its own shareholders, but have a systemic affect on other banks. Therefore, it is important to ensure that banks are operating properly. Carse also stated that the corporate governance of banks in Hong Kong is at a good standard due to the fact that the Hong Kong Monetary Authority has set out strict guideline in relation to corporate governance for banks.

On the other hand, a large number of studies have investigated the relationship between ownership structure and firm performance. Morck, Shleifer, and Vishny (1998) argued that higher ownership concentration has a positive impact on firm performance, because it increases the ability of shareholders to properly monitoring managers. Shleifer and Vishney (1986) also argued that higher level of block-holder is likely to have a positive effect on firm value. The large shareholders can work effectively for monitoring managers in order to prevent the potential takeover threat.

Based on the corporate governance structure, the board of directors will be the supreme policy maker in a company, so the relationship between structure of board composition and firm performance is extremely close. As we know board composition is part of the corporate governance, so our research takes a step forward to evaluate the relationship between board composition and firm performance.

Board composition and firm performance

Stanwick and Stanwick (2005) argued that members on the board of directors of banks are important for the bank's long term performance. Board of directors is a collective of people who are nominated by the shareholders of a company, and responsible for making decisions and supervising the daily operations of the firm. The existence of board of directors is very essential and necessary. As in daily operation, it is very hard to make detailed decisions through shareholders' regular meetings, especially for the public-listed companies which have a large number of shareholders. With proper of supervision of the firm's operation, board of directors ensures that the corporation operates in the direction that benefits the shareholders.

Moreover, Carse (2000) stated that the board of directors must play a role in approving the strategy and business plans of the bank. Board of directors must monitor the performance of management well to ensure that that the bank operates its business with high ethical standards. According to the Hong Kong Monetary Authority (HKMA) (2000), a board of directors should contain a mixture of both executive and non-executive independent directors. It also

requires the separation roles of Chairman of the board of directors and Chief Executive Officer (CEO) of the company.

According to the Stock Exchange of Hong Kong Limited (1989), company directors in Hong Kong must comply with the company ordinance under the governance rules listed on the Stock Exchange of Hong Kong Limited. According to the HKMA (2000), an independent non executive director is required for Board of banks in order to maintain the independence in corporate governance. It believed that an effective board of directors will protect the shareholders' rights by adopting strategies to ensure the structure of the corporation (Famma and Jensen, 1983).

In a recent study of the corporate governance in the Hong Kong banking industry, Tsui and Gul (2000) argued that the quality of the members in the board of directors is more important to achieve a high corporate governance standard. They investigated a number of boards of directors of the listed banks in Hong Kong, and found that board where the majority of directors hold at least Master degrees are perceived to be of a high standard.

According to Jensen and Meckling's (1976) convergence-of-interest hypothesis, when the shareholding ratio of the board of directors exceed a certain amount, the directors' self-interest and the company's interest will be integrated. This will give the board of directors more incentives on supervision of the management team's activities, and hence improve the performance of the firm. The same result was reported in Kesner’s study (1987), where the higher the shareholding ratio, the more incentives for the board, and the better the firm performance.

On the other hand, members of the board of directors may have their own interests in the company. They may use the company's resources to acquire the company or to reject public open offers of acquisition due to their own interests (Jensen and Ruback, 1983). Allen and Cebenoyan (1991) found that listed banks were more likely to make acquisitions that would add value to the banks when the ownership concentration is low. These studies are referred to as the entrenchment hypothesis, that is, when the share rights are highly controlled by the board, the possibility of entrenchment is higher as well, which leads to poor firm performance.

Morck, Shleifer and Vishny (1988) analyze firm performance measured by Tobin's Q and found that the Tobin's Q increases in the early stage-indicating a positive association between the share structure and the firm value; and decreases in the later stage, indicating a negative relation between the share structure and firm value. In other words, the relationship between share structure and Tobin's Q is non-linear concluding, the effects of convergence of

interest and entrenchment can give rise to different relationships between ownership structure and firms performance.

Board size and firm performance

From research on effect of board size in small and medium sized firms, Bennedsen et al (2008) concluded that effect of board size on performance given by a causal interpretation. Based on these findings, no performance effects were found when varying the board size at levels below six directors, the typical range of board size in small and medium-sized firms, but a negative board size effect in boards of seven or more members was found (Bennedsen et al., 2008). As an adequate size of board lead to an effective monitoring, finding the right number of directors is a trade-off between the benefits of having sufficient competencies represented and the cost arising from increased free riding among directors (Bennedsen et al., 2008). Another result on Nigerian stock exchange also shows that the size of the firm has a positive impact on firm performance. This suggests that firms with larger boards outperform compared to firms with small boards (Ehikioya, 2009). On the other hand, the study on the impact of corporate governance mechanisms on the firm value shows an inverse relationship between board size and firm value and suggests that the negative relationship between board size and firm value transcends different corporate governance systems (Mak & Kusnadi, 2005). However, the results made through for all OECD countries indicate that there is no a negative relationship between firm value and the size of the board of directors (Andres et al., 2005).

Board activity and firm performance

Board activity, which is referred as board meeting frequency, is an important dimension of board operations. The empirical study for Chinese listed firms during 2003-2004 found that the frequency of board meetings is negatively associated with firm value, while the frequency of general shareholder meetings is positively associated with firm value (Ma & Tian, 2009). They argue that frequent board meetings imply internal problems or inefficient decision-making while frequent general shareholder meetings display both confidence on the firm's management and an acceptance of broad suggestions (Ma & Tian, 2009). With the same conclusion, the investigation of 307 firms over the 1990-1994 period shows that the annual number of board meetings is inversely related to firm value because ofincreases in board activity following share price declines (Vafeas N., 1999).

There are only a few studies on corporate governance and productivity conducted in Nepal. Andenas *et.al.* (1999) are concerned with financial reporting and corporate governance in Nepal. The study focuses on transparency, accountability and enforcement. Adam Smith Institute (1999) identifies, for policy suggestions and legislation, some key issues that need to be addressed in order to improve the performance of state enterprises in the country.

Corporate Governance and Regulation in Nepal

Banking system of Nepal is gearing up for different business and economic environment. Nepal Government and central bank are working to develop transparent, competitive and strong financial sector. Till date, there have been several efforts towards building regulatory mechanism for corporate governance. Among those several efforts following are the acts and regulations, which provide necessary guidelines to maintain corporate governance in the bank and financial institutions.

1. Banks and Financial Institutions Act 2063
2. Directive 6 issued by the NRB
3. Companies Act 2063

Banks and Financial Institutions Act 2063 (BAFIA 2063)

(i) Conflict of Interest and Transparency

- Section 48-Restriction to give loans to promoter, director, executive officer etc
- Restriction on dealing with shares by the directors, Officers of the Bank(s.11)
- Disclosure requirement for directors regarding conflict in appointment of auditors, shareholding by family members, transactions between bank and family members (s.22)
- Directors not to take personal benefit (s.24)
- Disqualification of auditors and duty of the auditors (s.61 and s.63)
- Remuneration of directors to be as provided in the articles of association (s.21)

(ii) Competent Key Personnel

- Qualification of directors and chief executive officers (s.18,s.26)
- Requirement to appoint professional director(s.13)

NRB Directive 6

Code of Conduct for Directors

- Directors should not interfere in day-to-day operation of the financial institution.
- If there is a conflict, director needs to inform the board before assuming office.
- Directors should not involve in any activity which is against the interest of the company (conflict of interest)
- Chief executive should work fulltime.
- Directors of one deposit taking institution cannot act as director of other FI.
- Director Can not act as custodian or trustee of any of the customer
- Director shall not misuse its position and should deal fairly
- Director should keep up to date and accurate record of accounts and reports
- Director should not use or misuse information received from clients for person benefit
- Outlines the duties and responsibilities of the directors
- Provides additional disqualification for the appointment of chief executive directors
- Provides for code of conduct to be followed by the chief executive and other employees.

Audit Committee

- Headed non executive director
- Outlines responsibilities of the audit committee

- Restriction on granting of loan to directors, shareholders, employees and firm related to such persons. (Conflict of interest)

Companies Act 2063

(i) Conflict of Interest and Transparency

- Requirement to give beneficial interest on the shares(s.47)
- Information required to be given on becoming substantial shareholder (s.50)
- Shareholders having conflict are not qualified to vote in general meetings(s.70)
- Director required to give information about transaction between company and him/her or close relatives (s. 92)
- Approval of general meeting required to enter transaction between company and director/its close relatives (s.93)
- Restriction on power of board to enter certain transaction (s. 105)
- Restriction to give loans to directors and officers (s.101)
- Financial disclosures to the shareholders (s.109)

(ii) Directors

- Directors are made personally liable for any breach of the Act
- Directors have fiduciary duty to act in the best interest of the company (s.99)
- Directors are specific duty not to exceed their powers (s.103)
- Requirement to appoint independent directors by public companies (s. 86)
- Directors who breach reporting requirement under the Act are disqualified to become director (s.89)

(iii) Audit

- Listed companies having paid up capital of more than Rs. 3 crores need to have audit committee

- An auditor is disqualified to be appointed for three consecutive years.(111)
- A person working full time, or his/her partners are disqualified to be appointed as auditor (112)

(iv) Shareholders' Protection.

- Shareholder have right to inspect books of the company
- Shareholders can sue on behalf of the company.(s.140)
- Shareholders can request to appoint investigation officer (s.121)
- Can prevent directors from exceeding their powers.(s.138)

2.3 Theoretical framework

2.3.1 Board size

Board size refers to the number of directors in the board. The number of board members is different from country to country or corporate to corporate, because of the differences in culture, regulation, and corporate ownership structure (Wu, 2009). According to CG Principles, to obtain an effective monitoring, the board should be adequately sized. In Nepal, Law on Enterprises regulates that number of directors on boards cannot be less than 5 and more than 11 members (Nepal Company Act, 2063). In addition, empirical analyses suggest a positive relationship with optimal board size ranging from 5 to 10 members.

2.3.2 Board activity

There are many kinds of activity of the board in leading and monitoring the company. This study measures board activity based on the frequency of board meeting hold in a year. Since the frequency of board's meetings can represent for how effective the board has been in monitoring management and absolutely an effective board no need to hold meetings very often. Hence, board of directors with a proper frequency of board meetings enhances the efficiency of firm management and adds to firm value. Importantly boards that meet more frequently are valued less by the market, a finding that seems to be driven by share price declines being followed by higher meeting frequencies (Vafeas, 1999). However, sometimes an abnormally high meeting frequency is followed by improvements in operation performance and impact positively on firm performance (Vafeas, 1999).

2.3.3 Ownership concentration

Transparency of ownership structure is more and more important. As discussed, good CG used to reduce the agency problem between owners and managers and the conflicts of interests resulting from the separation of ownership and control. We cannot deny that agency problems have been created from conflicts between interests of owners and agent or poor corporate governance implication. Ownership concentration shows how concentrated in possession of outstanding shares, for example a concentrated ownership indicated a few owners hold a large portion of shares. Therefore, it is argued that concentrated ownership can reduce the agency problems since few large owners will monitor the firm more closely and efficiently. However, in case just one or two members hold a very large portion of shares, they have tendency to act according to their own objectives rather than minority shareholders and can cause the lower value of firm. It is not strange when Lefort & Urzua (2008) believe that in companies with high ownership concentration, the most pervasive agency conflict in the firm is between controlling shareholders and minority shareholders, the so-called horizontal agency problem (Lefort & Urzua, 2008). In addition, boards of companies with high ownership concentration will tend to be mostly comprised of directors who represent the owner manager's interests, thus being unable to deal with the specific agency problem adequately (Lefort & Urzua, 2008). In Vietnam, there are still a lot of companies in which the state hold a significant shares and in consequence, those companies usually get a better support from political and social strategies.

Bank Size

Bank characteristics have potential effects on how corporate governance impacts performance. In order to control for bank characteristics, this study has constructed variable to proxy for bank size. Bank size is generally used to capture potential economies or diseconomies of scale in the banking sector. Scale efficiencies can improve bank efficiency as the unit cost of production falls with increased size. Furthermore, it may increase net efficiency through improvements in efficiency that involves superior combinations of inputs and outputs resulting from larger size. Finally, it may improve efficiency through the exercise of additional market power in setting prices (Molyneux and Iqbal, 2005).Therefore, increasing size could lead to improve performance, if there are significant economies of scale (see Akhavein et al. 1997; Bourke, 1989; Molyneux and Thornton, 1992; Bikker and Hu, 2002;Goddard et al., 2004). In the other hand, if increased size leads to diversification and lower credit riskthis could lead to negative impact on banks performance.

Empirical studies in banking efficiency, conclude that few cost savings can be achieved by increasing the size of a banking firm, especially as markets develop (Boyd and Runkle, 1993; Millerand Noulas, 1997; Athanasoglou et al., 2005). Such a relationship is expected to be observed in Nepalese banking systems, which hire high quality and, therefore, relatively high cost staff. Hence, providing that the high quality staff is sufficiently productive, such banks will not be disadvantaged from a relative efficiency point of view.

From all the literature that is reviewed in this study concludes that the banks with smaller size of board will exhibit more corporate governance responsibility than banks with larger size of board member; board of directors with a proper frequency of board meetings enhances the efficiency of firm management and adds to firm value; the number of shareholders will determine the strength of decision reached at the end of each year's meeting. It is argued that concentrated ownership can reduce the agency problems since few large owners will monitor the firm more closely and efficiently. However, in case just one or two members hold a very large portion of shares, they have tendency to act according to their own objectives rather than minority shareholders and can cause the lower value of firm. Bank size is generally used to capture potential economies or diseconomies of scale in the banking sector. Scale efficiencies can improve bank efficiency as the unit cost of production falls with increased size. Therefore, increasing size could lead to improve performance, if there are significant economies of scale.

Research methodology is related to the specific problem of limited scope for which management has need of additional information on which to base a decision. Research methodology mainly describes the technique, method and process applied in the entire process of a scientific research. So, in this chapter the study will introduce how to get started to do this study from collecting data, retrieving necessary information, building the frame of variables to researching philosophy or approaching method.

3.1 Research Design

The research design includes specification of the method of the purposed study and detailed play for carrying out the study with various empirical data for the analysis of the problem. Therefore, this section describes the variable of interest used in this study. This study also attempted to formulate a model that will guide the study in its analysis. The study used Return on Assets (ROA), Return on Equity (ROE and Non-Performing loans (NPL) as the variables that measure bank performance. The number/size of Board of Directors (SBOD), the Number of Shareholders (CBOD) and measures the corporate governance index, while total Assets and Total Equity served as control variables (Berger etal, 2004). These variables will be defined shortly. The study shall utilize the descriptive and correlation analysis to examine the relationship between Corporate Governance and Bank Performance in Nepal.

3.2 Nature and Sources of Data

This study is primarily based on secondary sources of data. The required data that will be used for this study will be obtained from the annual reports of 22 out of 32 commercial banks (69%) operating in Nepal, Nepal Rastra Bank's supervision report and also from the website of Nepal stock exchange. Also differed books from library, periodicals, newspaper cuttings, company's magazines are used as per the requirement. Needless to say that this study is associated with past phenomena, therefore, only secondary data is used to carry out the whole calculations.

3.3 Population and Samples

The 32 'A' class commercial banks of Nepal are populated of this study whereas 22 banks are taken as samples.

In order to examine the role of corporate governance in bank performance, this study is based on a sample of 22 commercial banks of Nepal with the period from 2007 to 2011. Corporate Governance data were estimated by using public available documents and website disclosure. The accounting data used in these models were extracted from the concerned bank annual reports and NRB supervision report. Specifically, this study sample contains 15 domestic private banks (DPB) 7 joint venture banks (JVB). Unfortunately, this study excluded the public owned banks because of lack of all the appropriate information for our model.

Table 3.1: Lists of bank selected for the study

S. No.	Bank Name	Number of year	Type of Bank
1	Bank of Aisa	4	DPB
2	Bank of Kathmandu	5	DPB
3	Citizen Bank Limited	5	DPB
4	Everest Bank limited	5	JVB

5	Global Bank Limited	5	DPB
6	Grand Bank	5	DPB
7	Himalayan Bank Limited	5	JVB
8	KIST Bank Limited	3	DPB
9	Kumari Bank Limited	5	DPB
10	Laxmi Bank Limited	5	DPB
11	Lumbini Bank Limited	5	DPB
12	Machhapuchure Bank Limited	5	DPB
13	NABIL Bank Limited	5	JVB
14	Nepal Bangladesh Bank	5	JVB
15	Nepal Investment Bank Limited	5	DPB
16	Nepal SBI	5	JVB
17	NIC Bank Limited	5	DPB
18	NMB Bank	5	JVB
19	Prime Commercial Bank Limited	4	DPB
20	Siddhartha Bank Limited	5	DPB
21	Standard Charted Bank Limited	5	JVB
22	Sunrise Bank	4	DPB

Source: NRB Supervision Report

3.4 Method of Analysis

In order to analyze the study this study uses the descriptive analysis, coreelation analysis and the linear regression analysis by using the model given below:

Model Specification

To investigate the relationship of bank profitability in term of ROE, ROA, NPL with Board Size, Total Assets, and Total Equity regression model is used. The basic regression can be expressed as:

MODEL: 1

$Perf_{it} = \beta_0 + \beta_{1t} + \beta_{2t} + \partial_{1t} + \partial_{2t}$ …… (1)

Where,

- Perf indicates the performance variables: ROA, ROE, and NPL
- Subscript it, represent the bank i at time t.
- β_{1t} represent Size of the Board of Director (SCOS)
- β_{2t} represent Number of Shareholders (SHOD)
- ∂_{1t} represent total assets (TA)
- ∂_{2t} represent total equity (TE).

MODEL 2:

$$Y_{it} = \beta_0 + \beta_1 X1_{it} + \beta_2 X2_{it} + \beta_3 X3_{it} + \beta_4 X4_{it} + \beta_5 X5_{it} + u_{it} \ldots\ldots\ldots\ldots (2)$$

Where;

- Y_{it} represents Return on Asset (ROA) and Non-Performing Loan (NPL) for firm i at time t.
- $X1_{it}$ represents firm's board size for firm i at time t
- $X2_{it}$ represents frequency of board meeting for firm i at time t
- $X3_{it}$ represents firm's size (SIZE) for firm i at time t
- $X4_{it}$ represents LEVERAGE for firm i at time t
- $X5_{it}$ represents ratio of GROWTH for firm i at time t
- u_{it} = Error term.

- **Definition of Variables**

a. Bank Performance

As stated before in review of literature, the financial ratios are used to reflect the performance of the companies. There are many measuring factors in financial literature such as Tobin's Q, return on equity, return on asset, return on sale, nonperforming loan and so on.

The measures of bank performance used in this study are: Return on assets (ROA), Return on equity (ROE), and Non-performing Loans (NPL)

Return on Assets

ROA equals after tax net income divided by average total assets of a bank. This aims to examine the amount of after tax net income that can be earned for every naira of assets in the bank. The ration reflects whether the bank uses assets

effectively in order to produce its income, so it is an important profitability indicator

$$ROA = \frac{Net\ Profit\ after\ taxes}{Total\ Assets}$$

Return on Equity (ROE)

ROE equals after tax net income divided by average total equity of a bank. This aims to examine the amount of after tax net income that can be earned for every naira of equity.

It indicates the amount of income that shareholders will earn in a bank. It must be understood that an increase in ROE due to an increase in leverage may be an issue of concern for the bank's management.

$$ROE = \frac{Net\ Profit\ after\ taxes}{Total\ Equity}$$

Non-Performing Loans

Credit business is the main business for commercial banks. Since banks use a large portion of their funds for providing credit to firms and individuals, so they face the possibility that firms or individuals may sometimes show unwillingness to repay such borrowed funds promptly. This attitude often exposes banks to losses from providing credit business.

$$NPL = \frac{Non\ Performing\ Loan}{Total\ Loan}$$

b. Corporate Governance Variables

The measure of corporate governance used in this study are size of the board of directors (SCOS), number of shareholders (SHOD) and Board Activity (BM) in the firm.

Size of Board of Directors

Regards to the board size & composition variables, the number of directors (*SCOS*) is the total number of directors on a board. It is clear that large board size is associated with sufficient capacity to monitor the company and lower efficiency due to the time consumed in reaching agreements (Ma & Tian, 2009). However, many studies have concluded inconclusive results from different markets, for example, Yermack (1996) has stated his main finding of an inverse association between board size and firm value when evaluating US public corporation (Yermack, 1996); conversely, Cheng (2008) provides empirical evidence that firms with larger boards have lower variability of corporate performance. This relationship between board size & composition and firm performance is discussed more in the chapter 2.

Size of board of directors is the total number of members within the board of directors. This study will examine the extent to which the bank performance will be affected by the size of the board of directors. It is expected that banks with smaller size of board will exhibit more corporate governance responsibility than banks with larger size of board member.

Number of Shareholders

This represents the total number of shareholders within a bank. It is also known that banks are expected to have their AGM at the least once every year. Thus the number of shareholders will determine the strength of decision reached at the end of each year's meeting

Board Activity

Meeting is a very necessary part of any company. All the problems are discussed and the solutions are drawn from it. As per the bank and financial institution act a bank must have at least 12 boards meeting in a year. The frequency of board meeting means the meeting held by the board members and there is only a presence of board members in the meeting.

Board's activity, which referred as the number of board's meeting per year (*BM*), reflects how much involvement that the board contributes in monitoring since the board has right to decide on important issues and supervise board of management. Thus, a proper frequency of board meetings may enhances the vigilance and oversight of firm management and adds to firm value and alternatively (Ma & Tian, 2009).

c. Control Variables

The control variables used in this study are total assets of the bank and total equity of the banks.

Total Assets

This variable could also be used to measure the size of the bank. It is expected that larger banks will perform better, because they may have more diversified investment opportunities, better management, and employ better technology.

Total Equity

This variable can also measure the amount of shareholders fund in the bank compared to the average shareholders' funds in the industry. It is expected that banks with greater equity should perform better than banks with smaller equity.

Firm size: It is natural logarithm of total assets.

Leverage: It is book value of debt divided by book value of total asset

$$Leverage = \frac{Total\ Debt}{Total\ Assets}$$

Growth: It is growth rate of Total Operating Revenue. The growth of the total operating revenue is calculated as below:

$$Growth_n = \frac{TOR_n - TOR_{(n-1)}}{TOR_{(n-1)}}$$

CHAPTER 4: PRESENTATION & ANALYSIS OF DATA

The data used for this research was pooled from the bank's annual report which was obtained from the respective website. After compiling this data, a descriptive statistics, correlation and multiple panels linear regression analysis is carried out on the return on assets (ROA), return on equity (ROE) and non performing loans (NPL) ratios. This is to ensure that the mean, median and standard deviation of this data is analyzed as well as the impact of the ownership variables on the performance ratios. The trend revealed from the descriptive analysis as well as the regression model results ought to depict a general trend of the Nepalese banking industry. Finally, from the regression model, it is determined if a relationship exists between ownership and banks' performance in Nepal.

It has three sections. The first section is the descriptive statistics which summarizes the main features of the study variable such as mean, maximum, minimum and standard deviation. The second section is the correlation analysis which shows the degree of association between the study variables. The third sections of the chapter, regression results report the OLS estimation output of the five regression models (Multivariate Analysis).

4.1 Relationship between corporate governance and Bank's profitability (Descriptive Interpretation)

Table 4.1: Summary of Description Statistics

	No. of Obser.	Minimum	Maximum	Mean	Std. Deviation	Median
ROE	105	-.0819	1.9403	.189408	.2219372	0.1613
ROA	105	-.1463	.1804	.016290	.0260511	0.0143
NPL	105	.0000	.3976	.025947	.0592266	0.0092
SCOS	105	5.00	10.00	7.6857	1.17926	8.0000
SHOD	105	.00	4.90	3.8626	1.17015	4.1600
TA	105	9.47	10.77	10.2300	.29508	10.2400
TE	105	.00	9.71	8.9470	1.56035	9.2400
SIZE	105	9.47	10.77	10.2300	.29508	10.2400
LEVERAGE	105	.7436	1.3617	.910641	.0683660	0.9131
GROWTH	105	.0000	8.2929	.463978	.9646628	0.2481
BM	105	2.00	22.00	13.0952	2.57400	12.0000

Source: Appendix

This section discussed the summery statistics of each variables of the study. The variables include the dependent, independent and control variables. The dependent variables used in this study in order to measure the sample commercial banks financial performance are: return on asset, return on equity and non performing loan whereas the explanatory (governance) variables are board size, board members and board meeting. In addition to the explanatory variables control variables were included those are bank size, log of total equity, banks leverage and banks growth (measured by growth of total operative revenue). Accordingly, the descriptive statistics for all variables are presented above in table 4.1.

As we can see, the return on asset ROA of 22 commercial banks is 0.016290 on average. The return on asset varies in a wide range from a minimum of -0.1463 to a maximum of 0.1804. As the minimum value being negative indicates that some banks have also incurred losses during the sample period.

The average return on equity (ROE) of the sample bank is 0.1894 (i.e. 18.94%) which is close to the median value of 0.1613 (i.e. 16.13%). It varies widely from minimum -0.0819 to maximum 1.9403 (i.e. 194.03%). The reason behind this result is that in the period of the sample the bank has incur losses due to which the minimum value falls to negative and the maximum value crosses above 100% due to the negative reserve and surplus which reduces the equity amount at very low point.

The financial performance of the sample commercial banks on average is 2.59 percent (mean=0.025947) as measured by non performing loan. The maximum value of nonperforming loan among the sampled commercial banks is 39.76 percent and the minimum value is 0.00 percent. It shows a standard deviation of 5.92 percent from the mean value.

From the three indicators of financial performance in table 4.1 above, return on equity is first, non performing loan is second and return on asset is the last, when they are ranked from the highest to the lowest value in terms of their mean and maximum values. On the bases of standard deviation from the mean, return on equity shows higher standard deviation i.e. 22.19 percent. However the deviation of return on asset and non performing loan is 2.6 and 5.92 percent, which is low in comparison with return on equity. Generally, the three financial performance indicators do not have the same value in different aspects of descriptive statistics indicators.

The number of director has a mean of 7.68 and median of 8. The range of number of director is not much with largest board has 10 directors and the smallest one has 5 directors. The range of this variable seems to conform to Company Act 2063. The median of number of director is 8 means that higher percentage of companies was found to have nearly average number of board in range of (7-8) and higher percentage of banks have number of board in range (5-10). It proves that board of director in Nepal favors the board with average number of people. However, according to CG Rules and empirical studies, board size of public joint stock companies should be sufficient but not too many members to allow effective operations.

Besides, number of board meeting varies in a wide range from 2 to 22 times per year. Board meeting hold at least once a year, but for some boards, they hold meetings more frequently up to 22 times a year. On average, the board of directors holds meetings about 13 times a year. As indicated from the Bank and Financial Institution Act2002, board requires meeting at least 12 and board meetings attendance should be disclosed. However, this rule is not properly compiled. Besides, since almost banks in Nepal hold once annual shareholders meetings per year, therefore this kind of variable is not considered as a factor of board’s activity influencing firm performance in this study.

The mean value of bank size as measured by the natural logarithm of total asset is 10.23 (NPR 16982.44 in millions) with having a maximum value of 10.77 (NPR 58884.37 in millions) and a minimum values of 9.47 (NPR 2951.21 millions). The standard deviation of bank size among the sample commercial bank is 29.51. On the other hand, the leverage of selected commercial banks in Ethiopia is 91.06 percent on average as measured by debt to asset with a range of 74 to 136 percent. There is a low deviation, 6 percent, from the mean value of the bank's leverage. Finally, the sample commercial banks growth has 46 percent average value for the study period. The standard deviation of bank growth rate indicates a high variation of 96 percent among the sampled commercial banks. The maximum and minimum values of bank growth rate are 829 and 0 percent respectively among the sampled commercial banks. Also the total equity value which is also measured by natural logarithm has a minimum value of 9 due to the negative amount of the equity of any one of the sample bank where as the mean value of the equity is 8.95 (NPR in millions).

4.2 Correlation analysis of the Corporate Governance and Bank's Profitability

This section of the study presents the results and discussions of the Pearson correlation analysis. To identify the relationship among the variables of corporate governance and financial performance of Pearson correlation coefficients were used. The correlation coefficients show the extent and direction of the linear relationship between corporate governance variables and financial performance measures of the sample Nepalese commercial banks. The correlation analysis has three sub-sections. The first sub-section shows the relationship between return on asset and selected corporate governance variables. The second sub-section is about the association between return on equity and corporate governance variables. Finally, the relationship between non performing loan and corporate governance variables were analyzed. The

probability is shown in parenthesis with the correlation coefficient for the three correlation matrix below. The significance level also shown that is ***, ** and * for 1%, 5% and 10% level respectively. The correlation coefficients are checked for the presence of high co linearity among repressors. Since the correlation analysis shows only the degree of association, it is followed by multiple regression analysis.

4.2.1 Correlation Analysis of ROA and Corporate Governance Mechanisms

Below in table 4.2, the correlation matrix which shows the relationship of the return on asset with board size, number of shareholders, board meetings, Total Equity, bank size, bank's leverage and bank growth. This table also shows the linear relationships between each independent variables and control variables used in this study.

Table 4.2 point out that total equity is positively and significantly correlated at 1 percent significance level with return on asset. On the other hand, leverage is negatively and significantly correlated at 10 percent significance level with return on asset. However, board size, number of shareholder, bank size and frequency of board meeting shows insignificant correlation with return on asset. Even though they are not significant number of shareholder, bank size and frequency of board meeting shows a positive coefficient and board size shows a negative coefficient as expected.

As per the correlation result reported in table 4.2, the Pearson correlation coefficients of board size, board meetings, and numbers of shareholders are -3 percent, 0.6 percent, 16 percent, respectively. From this it can be understand that this variable do not so very strong association with return on asset.

4.2.2 Correlation Analysis of ROE and Corporate Governance Mechanisms

Below table 4.2 presents the Pearson correlations among return on equity and corporate governance mechanisms as well as control variables of the study. Here, also the independent variables are board size, number of shareholders, and

board meeting. The control variables are bank size, banks financial leverage, total equity and bank growth. As shown in table 4.2 below, number of shareholder is positively related with return on equity at 1 percent significance level. The board meetings and board size are negatively correlated but does not have a significant relation with return on equity.

4.2.3 Correlation Analysis of NPL and Corporate Governance Mechanisms

Below, Table 4.2 also shows, the correlation matrix that predicts the likely relationship of the non performing loan with board size, number of shareholder, and board meeting as independent variables and bank size, total equity, banks leverage and bank growth as control variables of the study.

Based on the Pearson correlation independent variables; board size, number of shareholder, and board meeting shows statistically insignificant correlation with nonperforming loan. Bank growth is the only control variable which is statistically not significant.

The bank size, total equity and bank leverage shows the significant relation where leverage shows the positive correlation and significant at the level of 5%, bank size and total equity shows the negative correlation and statistically significant at the level of 1 percent and 5 percent respectively.

From the correlation coefficients of the three models, shown in table 4.2, no high correlation is found among the independent as well as control variables. All the independent and control variables included in the three models are not strongly correlated with each other that results multi-collinearity problem since all the coefficients are lower than 0.8.

Table 4.2: Correlations among the variables

		ROE	ROA	NPL	SCOS	SHOD	TA	TE	SIZE	LEVERAGE	GROWTH	BM
ROE	Pearson Correlation	1	.729**	.243*	-.066	.193*	.172	.147	.172	.014	-.090	-.068
	Sig. (2-tailed)		.000	.013	.503	.048	.079	.134	.079	.888	.361	.492
	N	105	105	105	105	105	105	105	105	105	105	105
ROA	Pearson Correlation	.729**	1	.015	-.030	.159	.109	.223*	.109	-.303**	-.038	.006
	Sig. (2-tailed)	.000		.879	.761	.105	.267	.022	.267	.002	.701	.954
	N	105	105	105	105	105	105	105	105	105	105	105
NPL	Pearson Correlation	.243*	.015	1	-.098	.128	-.222*	-.814**	-.222*	.691**	-.072	.073
	Sig. (2-tailed)	.013	.879		.322	.194	.023	.000	.023	.000	.467	.457
	N	105	105	105	105	105	105	105	105	105	105	105
SCOS	Pearson Correlation	-.066	-.030	-.098	1	.057	.060	.065	.060	-.099	-.153	-.012
	Sig. (2-tailed)	.503	.761	.322		.566	.543	.508	.543	.317	.118	.902
	N	105	105	105	105	105	105	105	105	105	105	105
SHOD	Pearson Correlation	.193*	.159	.128	.057	1	.341**	.007	.341**	.096	-.341**	-.019
	Sig. (2-tailed)	.048	.105	.194	.566		.000	.942	.000	.328	.000	.851
	N	105	105	105	105	105	105	105	105	105	105	105
TA	Pearson Correlation	.172	.109	-.222*	.060	.341**	1	.344**	1.000**	.127	-.179	-.138
	Sig. (2-tailed)	.079	.267	.023	.543	.000		.000	0.000	.197	.068	.160

	N	105	105	105	105	105	105	105	105	105	105	105
TE	Pearson Correlation	.147	.223*	-.814**	.065	.007	.344**	1	.344**	-.771**	-.068	-.024
	Sig. (2-tailed)	.134	.022	.000	.508	.942	.000		.000	.000	.493	.807
	N	105	105	105	105	105	105	105	105	105	105	105
SIZE	Pearson Correlation	.172	.109	-.222*	.060	.341**	1.000**	.344**	1	.127	-.179	-.138
	Sig. (2-tailed)	.079	.267	.023	.543	.000	0.000	.000		.197	.068	.160
	N	105	105	105	105	105	105	105	105	105	105	105
LEVERAGE	Pearson Correlation	.014	-.303**	.691**	-.099	.096	.127	-.771**	.127	1	.037	-.051
	Sig. (2-tailed)	.888	.002	.000	.317	.328	.197	.000	.197		.706	.609
	N	105	105	105	105	105	105	105	105	105	105	105
GROWTH	Pearson Correlation	-.090	-.038	-.072	-.153	-.341**	-.179	-.068	-.179	.037	1	.175
	Sig. (2-tailed)	.361	.701	.467	.118	.000	.068	.493	.068	.706		.073
	N	105	105	105	105	105	105	105	105	105	105	105
BM	Pearson Correlation	-.068	.006	.073	-.012	-.019	-.138	-.024	-.138	-.051	.175	1
	Sig. (2-tailed)	.492	.954	.457	.902	.851	.160	.807	.160	.609	.073	
	N	105	105	105	105	105	105	105	105	105	105	105

**. Correlation is significant at the 0.01 level (2-tailed).

*. Correlation is significant at the 0.05 level (2-tailed).

4.3 Various Aspects of Corporate Governance Affecting Banks Performance and Profitability (Linear Regression)

Adjusted R^2 is used to compensate for the addition of variables to the model. As more independent variables are added to the regression model, unadjusted R^2 will generally increase but there will never be a decrease. This will occur even when the additional variables do little to help explain the dependent variable. To compensate for this, adjusted R^2 is corrected for the number of independent variables in the model. The result is an adjusted R^2 than can go up or down depending on whether the addition of another variable adds or does not add to the explanatory power of the model. Adjusted R^2 will always be lower than unadjusted.

The results of the ANOVA are presented in an ANOVA table. This table contains columns labeled "Source", "SS or Sum of Squares", "df - for degrees of freedom", "MS - for mean square", "F or F-ratio", and "p, prob, probability, sig., or sig. of F". The *t*-test tells us if the variation between two groups is "significant". In general, the purpose of analysis of variance (ANOVA) is to test for significant differences between means. Generally the level of significant is taken “1%”, “5%” and, “10%”.

Table 4.3: Summary of model 1 with ROE dependent variable

Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.266[a]	.071	.033	.2182060

a. Predictors: (Constant), TE, SHOD, SCOS, TA

ANOVA[a]

Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	.361	4	.090	1.897	.117[b]
	Residual	4.761	100	.048		
	Total	5.123	104			

a. Dependent Variable: ROE

b. Predictors: (Constant), TE, SHOD, SCOS, TA

Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	T	Sig.	95.0% Confidence Interval for B	
		B	Std. Error	Beta			Lower Bound	Upper Bound
1	(Constant)	-.550	.793		-.693	.490	-2.123	1.023
	SCOS	-.017	.018	-.089	-.915	.362	-.053	.019
	SHOD	.033	.020	.172	1.658	.101	-.006	.071
	TA	.057	.083	.076	.686	.494	-.107	.221
	TE	.018	.015	.126	1.214	.228	-.011	.047

a. Dependent Variable: ROE

This above table reports the regression analysis of ROE with number of shareholders, board size, total assets and total equity. It shows that the except for board size all other variable shows the positive relation but only number of shareholders shows a significant relation with the dependent variable which means that the higher the number of shareholders results in better bank performance (measured in terms of ROE). The regression result indicates that of 7.1% of the variation in ROA is determined by this independent variable. Also the ANOVA results shows that it is nearly significant at the level of 10 percent which means that the independent variable is nearly able to explain the dependent variable i.e. ROE by 7.1%. Therefore, the overall model is able to define the bank performance which is shown by the ANOVA table.

Table 4.4: Summary of model 1 with ROA dependent variable

Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.279[a]	.078	.041	.0255112

a. Predictors: (Constant), TE, SHOD, SCOS, TA

ANOVA[a]

Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	.005	4	.001	2.112	.085[b]
	Residual	.065	100	.001		
	Total	.071	104			

a. Dependent Variable: ROA

b. Predictors: (Constant), TE, SHOD, SCOS, TA

Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.	95.0% Confidence Interval for B	
		B	Std. Error	Beta			Lower Bound	Upper Bound
1	(Constant)	-.001	.093		-.012	.991	-.185	.183
	SCOS	-.001	.002	-.053	-.554	.581	-.005	.003
	SHOD	.004	.002	.169	1.640	.104	-.001	.008
	TA	-.002	.010	-.026	-.233	.816	-.021	.017
	TE	.004	.002	.234	2.268	.025	.000	.007

a. Dependent Variable: ROA

This above table reports the regression analysis of ROA with number of shareholders, board size, total assets and total equity. It shows that the board size and total assets have negative relation but both variable do not shows any significant relation as the level of significant for both the variable is above 50 percent. But the variable number of shareholders and the total equity shows the positive relation and also significant at the level of 10% and 5% respectively which means if any change in this variable will make a positive effect in the ROA i.e. increase in number of share holders and total equity will increase the ROA. The regression result indicates that 7.8% of the variation in ROA is determined by this independent variable. Also the f-static is significant at the level of 10 percent which means that the independent variable is able to explain the dependent variable i.e. ROE by 7.8%.

Table 4.5: Summary of model 1 with NPL dependent variable

Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.827[a]	.683	.671	.0339867

a. Predictors: (Constant), TE, SHOD, SCOS, TA

ANOVA[a]

Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	.249	4	.062	53.957	.000[b]
	Residual	.116	100	.001		
	Total	.365	104			

a. Dependent Variable: NPL

b. Predictors: (Constant), TE, SHOD, SCOS, TA

Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.	95.0% Confidence Interval for B	
		B	Std. Error	Beta			Lower Bound	Upper Bound
1	(Constant)	.262	.123		2.124	.036	.017	.507
	SCOS	-.003	.003	-.053	-.931	.354	-.008	.003
	SHOD	.007	.003	.131	2.161	.033	.001	.013
	TA	.004	.013	.018	.274	.785	-.022	.029
	TE	-.031	.002	-.818	-13.518	.000	-.036	-.026

a. Dependent Variable: NPL

The table 4.5 is the regression analysis of NPL with number of shareholders, board size, total assets and total equity. It shows that the number of shareholders and total equity are statistically significant at the level of 5% and the 1% respectively whereas the board size and total assets does not have significant relation. The number of shareholders has positive relation and significant with the NPL which means increase in number of shareholders increases the NPL and vice-versa whereas increase in total equity will lead to decrease in the bank performance which is measured in terms of nonperforming loan. The board size has negative relation and the total assets shows the positive relation with the bank performance based on nonperforming loan. The regression result from adjusted R square indicates that 67.1% of the variation in NPL is determined by this independent variable also it indicates the banks' performance based on non performing loan is affected by the response variables more than the half. Standard error of 0.03 shows that the coefficient estimate is reliable or that it has a small variability, which means that there are not many extreme prices in the model and thus, the trend is strong. Also the f-static is significant at the level of 1 percent which means that the independent variable is able to explain the dependent variable i.e. ROE by 67.1%. Therefore, from the overall model which is determined by the F-statistic probability zero leading to the rejection of the null hypothesis that all slope coefficients, except for the constant, are equal to zero and to the conclusion that the explanatory variables do have impact on the NPL.

Table 4.6: Summary of model 2 with ROA dependent variable

Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
2	.346[a]	.120	.075	.0250530

a. Predictors: (Constant), BM, SCOS, LEVERAGE, SIZE, GROWTH

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
2	Regression	.008	5	.002	2.690	.025[b]
	Residual	.062	99	.001		
	Total	.071	104			

a. Dependent Variable: ROA

b. Predictors: (Constant), BM, SCOS, LEVERAGE, SIZE, GROWTH

Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.	95.0% Confidence Interval for B	
		B	Std. Error	Beta			Lower Bound	Upper Bound
2	(Constant)	.001	.094		.016	.988	-.184	.187
	SCOS	-.002	.002	-.073	-.765	.446	-.006	.003
	SIZE	.014	.009	.155	1.594	.114	-.003	.031
	LEVERAGE	-.126	.037	-.329	-3.438	.001	-.198	-.053
	GROWTH	.000	.003	-.011	-.114	.910	-.006	.005
	BM	.000	.001	.012	.120	.905	-.002	.002

a. Dependent Variable: ROA

According to the Adjusted R–squared of Table 4.6, the model explains 7.5% of the variability of the dependent variable ROA. This means that the regression line does not approximates very well the real data points and thus, the model can predict less of the movements of ROA. Standard error of 0.025 shows that the coefficient estimate is reliable or that it has a small variability, which means that there are not many extreme prices in the model and thus, the trend is strong. It, also, presents the probability of F-statistic which is 0.025, meaning that the explanatory variables do have impact on the dependent variable.

With regard to the ROA regression output, there is a statistically positive relationship between the size and ROA at nearly 10% significance level whereas there is a negative relationship between leverage and ROA at a 1% significance level. So, ROA and thus performance is positively affected by the increase in size, by the debt used to finance the assets of the company. But the board size is

statistically insignificant and shows the negative relationship with the performance of bank measured in terms of nonperforming loan.

Table 4.7: Summary of model 2 with NPL dependent variable

Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
2	.781[a]	.610	.591	.0378978

a. Predictors: (Constant), BM, SCOS, LEVERAGE, SIZE, GROWTH

ANOVA[a]

Model		Sum of Squares	Df	Mean Square	F	Sig.
2	Regression	.223	5	.045	31.001	.000[b]
	Residual	.142	99	.001		
	Total	.365	104			

a. Dependent Variable: NPL

b. Predictors: (Constant), BM, SCOS, LEVERAGE, SIZE, GROWTH

Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	T	Sig.	95.0% Confidence Interval for B	
		B	Std. Error	Beta			Lower Bound	Upper Bound
2	(Constant)	.113	.142		.800	.425	-.168	.394
	SCOS	-.002	.003	-.031	-.485	.629	-.008	.005
	SIZE	-.067	.013	-.333	-5.147	.000	-.093	-.041
	LEVERAGE	.643	.055	.742	11.643	.000	.533	.753
	GROWTH	-.011	.004	-.181	-2.764	.007	-.019	-.003
	BM	.002	.001	.096	1.497	.137	-.001	.005

a. Dependent Variable: NPL

The table above presents the regression results having as dependent variable the non performing loan. The value of Adjusted R-squared is 0.591, so, the companies' performance based on non performing loan is affected by the response variables more than the half. The variability of the model is small as the standard error is close to zero. F-statistic gives a high value of 31.001, with

p-value showing zero, which leads us to reject the hypothesis that all slope coefficients are zero and to the conclusion that the explanatory variables do have impact on the NPL.

The table indicates that board meeting is having negative relation with NPL, while p-value does not overcome the 10% significance level. The leverage and the bank size are significant with 1% significance level indicating a very strong correlation in which leverage shows the positive relation whereas bank size shows the negative relation. With 90% confidence interval, the study observes a weaker correlation between the variables board size and NPL.

Corporate governance does not have strong relationship with Performance, as was detected before, which means that corporate governance's elements do not affect NPL. Multicollinearity is absent in this regression too, with tolerance not close to zero and VIF below 10. Standard errors of each variable are small, supporting the statistical reliability of the coefficients.

CHAPTER 5: SUMMARY, CONCLUSION & RECOMMENDATIONS

5.1 SUMMARY

Corporate governance will continue to have relevance to firms, as it constitutes the balance of power with which the organization is directed (Yakasai, 2001: 249). Corporate governance not only places the organization in an acceptable light with the public, but also affects other core areas of business such as profitability. Whilst company profitability is key, also important is how a company is viewed by the public, which ultimately affects the patronage it attracts from the public – its bottom line. This chapter reviews the results of the previous chapter and suggests areas of further research in this field and the likely positive effects on the performance of the firm.

Corporate governance is equally significance to all types of corporate institution. Furthermore it is very crucial and essential element for the banking system because bank and financial institutions depends on the Other Peoples Money (OPM). There may be a gap among major stakeholder like owners, depositors and management. Very limited people have a right to access in resources and decision. Due to the lack of transparency and adequate control mechanism, there may be the chance of vested interest and moral hazard problems. Nepal is a developing country and facing with the problem of political instability, low economic growth, and higher inflation. There is no any proper code of Corporate Governance prevailing in Nepal.

The general objective of this paper is to examine the relationship of different corporate governance variables on the profitability of the commercial banks in Nepal. The specific objectives are to investigate the relationship between corporate governance and profitability of banking sector, to explain the

relationship between corporate governance and banks performance in Nepal, to determine explicitly what variables explain corporate governance, to examine the impact of total assets on performance of the commercial banks of Nepal, to find out the impact of total equity on performance of the commercial banks of Nepal, and to examine the various aspects of corporate governance affecting bank's profitability that determines of board size and composition, shareholders, total assets and total equity.

The review of literature in this study shows that the banks with smaller size of board will exhibit more corporate governance responsibility than banks with larger size of board member; board of directors with a proper frequency of board meetings enhances the efficiency of firm management and adds to firm value; the number of shareholders will determine the strength of decision reached at the end of each year's meeting. It is argued that concentrated ownership can reduce the agency problems since few large owners will monitor the firm more closely and efficiently. However, in case just one or two members hold a very large portion of shares, they have tendency to act according to their own objectives rather than minority shareholders and can cause the lower value of firm. Bank size is generally used to capture potential economies or diseconomies of scale in the banking sector. Scale efficiencies can improve bank efficiency as the unit cost of production falls with increased size. Therefore, increasing size could lead to improve performance, if there are significant economies of scale.

This study try to figure out the relationship between corporate variables as defined by board size, board composition, board activity, board meeting, number of shareholders and firm performance and between the control variables bank size, total equity, growth of revenues and the leverage and firm performance for Nepalese commercial banks for the periods of five year (2007/008-2011/012). Descriptive analyses and a statistic overview on the range

of value for each variable are conducted to reach the objectives. The study uses correlation analysis, ANOVA analyses, and multiple regressions to test how these variables affect firm performance separately and connectedly. In this study, Return on Assets (ROA), Return on Equity (ROE) and Nonperforming Loan (NPL) are used as the measures for the bank performance.

This study has used 5 models to test the hypothesis. ROA, ROE, and NPL has been used as dependent variable and independent variables are member in Number of directors (board size), frequency of board meeting (board activity), number of shareholder, Logarithm of total assets, Logarithm of total equity, Growth of total revenue, total debt to book value of total assets Leverage).

From chapter 4 it shows that the model summary of first model of the study in which dependent variable is ROE. This model explains 7.1% of the variation of ROE. R square is 7.1% which indicates 7.1% relationship has been explained for dependent variable ROE by independent variables. Here the value of R square is weak. The F statistics by computing will test hypothesis that the explanatory variable helped explained variation in ROE about its mean. Here the F statistics is 1.897 and the model is nearly significance at the level of 10 percent. It shows that the except for board size all other variable shows the positive relation but only number of shareholders shows a significant relation with the dependent variable. Also, the summary of regression analysis of ROA with number of shareholders, board size, total assets and total equity is shown. It shows that the board size and total assets have negative relation but both variable do not shows any significant relation as the level of significant for both the variable is above 50 percent. But the variable number of shareholders and the total equity shows the positive relation and also significant at the level of 10% and 5% respectively. The nonperforming loan shows a better regression result then the other dependent variable in both models with adjusted R square being 67.1% and 59.1%. Also the ANOVA and f-static result shows that the model fits better for the nonperforming loan.

Therefore, the major findings of this study are as follows:

- The result of panel regression shows that the size of banks is negatively related to bank performance, indicating that the smaller bank, the better its performance will be.
- The number of meeting held is found to be negative to bank performance but coefficient is statistically not significant which means more meetings are not good on bank performance.
- The study reveals that board size has negative relationship with return on equity but it is statistically not significant.
- The board meeting does not show any significant result with the bank performance.
- As all models have very low standard error which means that the result of independent variable coefficient estimate is reliable or that it has a small variability.
- The regression result of bank performance measured in term of NPL is defined more than 50% by the independent variable.
- The total equity shows the negative but statistically significant relationship with the bank performance measured in terms of NPL.
- In all model the leverage is seem to show the significant result with the bank performance and also relationship is positive.
- The number of shareholder shows statistically positive significant relationship with the bank performance.
- The independent variables defining the bank performance based on ROA and ROE is very low but is statistically significant.
- The growth of total revenue shows negative relationship with the bank performance and also is statistically significant.

5.2 CONCLUSION

The study tested for the relationship between corporate governance and Bank performance in Nigeria between 2005 and 2008 using pool data which represent an expansion of existing research literature that can be equally applied elsewhere. The major conclusion of this study is that although Corporate Governance relationship with bank performance seems to be non – existent, but the output of overall models (i.e. ANOVA) shows the significant result and shows strong relationship of bank performance with a number of other financial variables. Specifically, this study has observed significant correlation of nonperforming loan as performance variables with Leverage and bank size as it was expected. This relationship is based on the fact that ROA, ROE, NPL, Leverage and bank size, growth are all financial ratios unbreakably connected with each other. Size, which was measured by the logarithm of Total Assets, is statistically significant with NPL ratio. The corporate governance variable that showed positive significance result with all dependent variables is number of shareholders.

5.3 RECOMMENDATIONS

For the purpose of future line of research, efforts should be put at increasing the sample size and the corporate governance variable, particularly the inclusion of leverage, board size, and other variables. More over the sample selection bias in favor of financial institution. It is hereby suggested that attention should be devoted to the study of manufacturing and non financial institutions.

Good corporate governance ensures that companies use their resources more efficiently and leads to better relations with workers, creditors, and other stakeholders. It is an important prerequisite for attracting the patient capital needed for sustained long-term economic growth. The firms should recognize and disclose the functions reserved to the board and those delegated to senior executives. Regular review of the balance of responsibilities may be appropriate to ensure that the division of functions remains appropriate to the needs of the

company. Companies should disclose the process for evaluating the performance of senior executives. A majority of the board should be independent directors.

Following the above argument, the study also recommends that the board size of banks in Nepal should not be too large and must be made up of qualified professional who are conversant with oversight function. There should also be a combination of self government regulation so as to detect rule violations and also monitor systemic problems for early solutions. The study frowns at the poor disclosure attitude of banks annual reporting. During the course of this study, the research did not find any element of disclosure regarding the amount of loans granted to bank directors. Thus, to enforce corporate governance principles, the banks should take the issue of transparency, accountability and disclosure more seriously.

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APPENDICES

Banks	YEAR	ROE	ROA	NPL	Size of board of directors	LnShareholder	LnTA	LnTE	Size	Leverage	Growth	Board Meeting
BOA	2007-08	0.0063	0.0021	0	9	0	9.63	8.85	9.63	0.8359	0	13
BOA	2008-09	0.0605	0.0077	0.0001	9	0	10.07	9.01	10.07	0.9127	2.6307	15
BOA	2009-10	0.1312	0.0153	0.0027	9	4.76	10.19	9.2	10.19	0.898	1.1864	19
BOA	2010-11	0.0974	0.0126	0.014	9	4.75	10.25	9.33	10.25	0.8783	0.1673	14
BOK	2006-07	0.2642	0.018	0.0251	6	4.28	10.16	9	10.16	0.9319	0.2035	12
BOK	2007-08	0.2694	0.0204	0.0186	6	4.28	10.25	9.13	10.25	0.9243	0.2745	12
BOK	2008-09	0.2651	0.0225	0.0127	6	4.33	10.31	9.24	10.31	0.915	0.2919	12
BOK	2009-10	0.2456	0.0218	0.0151	6	4.34	10.37	9.32	10.37	0.9114	0.2044	14
BOK	2010-11	0.2485	0.0244	0.0182	6	4.36	10.39	9.39	10.39	0.9016	0.1457	17
Citizen	2006-07	-0.0283	-0.0044	0	5	0	9.54	8.74	9.54	0.8438	0	13
Citizen	2007-08	0.0915	0.0075	0	5	0	9.86	8.78	9.86	0.9175	8.2929	16
Citizen	2008-09	0.0927	0.0074	0	6	0	10.11	9.01	10.11	0.9202	0.6893	14
Citize	200	0.14	0.01	0.0	7	4.81	10.	9.1	10.	0.920	0.75	16

n	9-10	8	17	031			22	2	22	8	8	
Citizen	2010-11	0.0913	0.0118	0.0117	8	4.81	10.23	9.34	10.23	0.8708	0.2044	14
Grand	2006-07	0.2162	0.0152	0.0267	9	4.2	9.47	8.54	9.47	0.883	0.2102	12
Grand	2007-08	0.0595	0.0112	0.0228	9	4.2	9.68	9.09	9.68	0.7436	0.3275	12
Grand	2008-09	0.0337	0.0115	0.0159	8	4.23	9.95	9.27	9.95	0.789	0.6377	12
Grand	2009-10	0.0786	0.0153	0.0144	8	4.25	10.01	9.31	10.01	0.8003	0.3116	12
Grand	2010-11	0.1046	0.0001	0.0195	8	4.25	10.1	9.33	10.1	0.8316	0.0876	12
EBL	2006-07	0.2467	0.014	0.008	8	4.19	10.33	9.08	10.33	0.9439	0.2706	12
EBL	2007-08	0.2349	0.02	0.0068	8	4.19	10.43	9.28	10.43	0.9292	0.4381	12
EBL	2008-09	0.2899	0.0173	0.0048	9	4.2	10.57	9.34	10.57	0.9403	0.2769	12
EBL	2009-10	0.3015	0.0209	0.0016	9	4.2	10.62	9.44	10.62	0.9333	0.2479	12
EBL	2010-11	0.2991	0.021	0.0034	8	4.29	10.66	9.49	10.66	0.9327	0.1374	12
Global	2006-07	-0.0819	-0.0115	0	6	0	9.55	8.67	9.55	0.8667	0	16
Global	2007-08	0.0847	0.0075	0.0085	6	4.75	9.92	8.86	9.92	0.9126	4.2038	15
Global	2008-09	0.053	0.0021	0	6	4.75	10.1	9.02	10.1	0.9169	0.7213	17
Global	2009-10	0.048	0.0042	0.009	6	4.75	10.24	9.18	10.24	0.9116	1	14
Glob	201	0.13	0.01	0.0	6	4.74	10.	9.2	10.	0.902	0.28	15

al	0-11	17	28	252			24	3	24	5	51	
HBL	2006-07	0.2291	0.0147	0.0361	8	3.89	10.53	9.33	10.53	0.936	0.07	12
HBL	2007-08	0.253	0.0176	0.0236	9	3.91	10.56	9.4	10.56	0.9305	0.1465	12
HBL	2008-09	0.2413	0.0191	0.0216	9	3.93	10.59	9.49	10.59	0.9207	0.2445	13
HBL	2009-10	0.1479	0.0119	0.0352	9	3.93	10.63	9.54	10.63	0.9195	0.0855	12
HBL	2010-11	0.2235	0.0191	0.0422	9	3.95	10.67	9.6	10.67	0.9145	0.1987	13
KIST	2008-09	0.0438	0.008	0.0022	7	3.75	10.05	9.31	10.05	0.8166	0	14
KIST	2009-10	0.069	0.0076	0.0019	7	3.83	10.28	9.32	10.28	0.8897	1.0259	15
KIST	2010-11	0.0252	0.0028	0.0254	7	3.84	10.28	9.33	10.28	0.8873	0.2925	13
Kumari	2006-07	0.166	0.0143	0.0073	8	4.05	10.08	9.01	10.08	0.9139	0.4211	12
Kumari	2007-08	0.1282	0.0116	0.0132	8	4.09	10.18	9.14	10.18	0.9092	0.2041	12
Kumari	2008-09	0.1609	0.0141	0.0044	7	4.14	10.27	9.21	10.27	0.9123	0.2643	12
Kumari	2009-10	0.1773	0.0159	0.005	8	4.15	10.31	9.25	10.31	0.913	0.2033	12
Kumari	2010-11	0.1135	0.0123	0.0112	8	4.16	10.31	9.35	10.31	0.892	0.0154	12
Laxmi	2006-07	0.0759	0.0095	0.0035	9	3.92	9.93	8.94	9.93	0.8993	0.4853	12
Laxmi	2007-08	0.1038	0.0113	0.0013	9	4.01	10.1	9.06	10.1	0.9089	0.5794	12
Laxm	200	0.14	0.01	0.0	10	4.03	10.	9.1	10.	0.926	0.40	12

i	8-09	07	22	008			26	3	26	9	82	
Laxmi	2009-10	0.171	0.0166	0.0012	9	4.03	10.32	9.28	10.32	0.9087	0.4986	12
Laxmi	2010-11	0.1775	0.017	0.009	10	4.02	10.33	9.32	10.33	0.902	0.153	12
Lumbini	2006-07	0	0.0337	0.2037	8	4.04	9.76	0	9.76	1.0753	1.8542	12
Lumbini	2007-08	1.1156	0.0536	0.1492	8	4.04	9.79	8.47	9.79	0.9523	0.2481	12
Lumbini	2008-09	0.3486	0.044	0.0906	8	4.06	9.88	8.98	9.88	0.8737	0.3371	12
Lumbini	2009-10	0.2089	0.041	0.0453	8	4.06	9.87	9.16	9.87	0.8036	0	12
Lumbini	2010-11	0.2107	0.0441	0.0096	8	4.07	9.95	9.27	9.95	0.7906	0.0429	12
MBL	2006-07	0.0762	0.0069	0.0116	6	4.05	10.03	9	10.03	0.9068	0	12
MBL	2007-08	0.0731	0.0068	0.0104	7	4.07	10.1	9.07	10.1	0.9069	0.2222	18
MBL	2008-09	0.0725	0.007	0.0233	7	4.11	10.24	9.23	10.24	0.9028	0.2327	16
MBL	2009-10	0.0413	0.0035	0.0232	7	4.11	10.32	9.25	10.32	0.9142	0.1308	16
MBL	2010-11	0.0046	0.0003	0.0446	9	4.11	10.31	9.25	10.31	0.9123	0	15
NBL	2006-07	0.3276	0.0272	0.0112	9	3.78	10.44	9.31	10.44	0.9245	0.0887	12
NBL	2007-08	0.3063	0.0232	0.0074	8	3.87	10.57	9.39	10.57	0.9344	0.1285	12
NBL	2008-09	0.3294	0.0255	0.008	7	3.92	10.64	9.5	10.64	0.9286	0.3296	12
NBL	200	0.29	0.02	0.0	8	3.98	10.	9.5	10.	0.926	0.24	9

	9-10	69	37	147			72	8	72	4	45	
NBL	2010-11	0.2922	0.0243	0.0177	8	4.01	10.76	9.66	10.76	0.9208	0.1078	16
NBBL	2006-07	0	-0.1463	0.3976	7	4.26	9.86	0	9.86	1.3617	0	14
NBBL	2007-08	0	0.0635	0.3173	7	4.3	9.97	0	9.97	1.2334	0.0285	14
NBBL	2008-09	1.9403	0.1804	0.198	7	4.34	10.08	9.05	10.08	0.907	0.5376	15
NBBL	2009-10	0.4787	0.0815	0.0647	7	4.36	10.1	9.33	10.1	0.8297	0	17
NBBL	2010-11	0.1838	0.0385	0.1918	7	4.36	10.2	9.35	10.2	0.8581	0.0277	20
NSBI	2006-07	0.2191	0.0183	0.0456	6	4.22	10.14	9.07	10.14	0.9163	0.1476	2
NSBI	2007-08	0.1751	0.0144	0.0383	6	4.23	10.24	9.15	10.24	0.9177	0.196	5
NSBI	2008-09	0.1847	0.0102	0.0202	6	4.26	10.49	9.23	10.49	0.9446	0.2987	8
NSBI	2009-10	0.1599	0.0103	0.0148	8	4.25	10.58	9.39	10.58	0.9356	0.3357	12
NSBI	2010-11	0.1613	0.0101	0.011	8	4.26	10.66	9.46	10.66	0.9375	0.2839	12
NIBL	2006-07	0.267	0.0179	0.0237	8	3.67	10.44	9.27	10.44	0.9319	0.2988	12
NIBL	2007-08	0.2593	0.0177	0.0112	8	3.78	10.59	9.43	10.59	0.9309	0.3239	12
NIBL	2008-09	0.2305	0.0168	0.0058	8	3.88	10.72	9.59	10.72	0.9263	0.2831	12
NIBL	2009-10	0.2761	0.0219	0.0062	8	3.9	10.76	9.66	10.76	0.92	0.2921	12
NIBL	201	0.22	0.02	0.0	8	3.92	10.	9.7	10.	0.911	0.03	12

	0-11	8	02	094			77	1	77	6	61	
NIC	2006-07	0.1725	0.0136	0.0111	7	4.51	10.07	8.96	10.07	0.9214	0.6786	12
NIC	2007-08	0.1865	0.0181	0.0086	7	4.5	10.18	9.12	10.18	0.9145	0.3296	14
NIC	2008-09	0.1912	0.0188	0.0023	7	4.54	10.27	9.22	10.27	0.9115	0.3177	13
NIC	2009-10	0.2549	0.023	0.0072	7	4.53	10.31	9.25	10.31	0.9131	0.3363	12
NIC	2010-11	0.2481	0.0234	0.006	7	4.53	10.34	9.3	10.34	0.9095	0.1681	12
NMB	2006-07	0.2641	0.017	0.0173	8	4.18	9.65	8.45	9.65	0.9357	0	15
NMB	2007-08	0.06	0.0082	0.0152	8	4.18	9.95	9.08	9.95	0.8641	0.0708	14
NMB	2008-09	0.0395	0	0.0051	8	4.21	10.2	9.2	10.2	0.8996	0.2612	15
NMB	2009-10	0.0883	0.0121	0.007	8	4.25	10.12	9.26	10.12	0.863	0.958	22
NMB	2010-11	0.1002	0.0139	0.0027	8	4.26	10.2	9.34	10.2	0.8613	0.2857	17
Prime	2007-08	0.0385	0.0044	0	9	2.59	9.81	8.86	9.81	0.886	0	12
Prime	2008-09	0.1386	0.0106	0	9	2.59	10.13	9.01	10.13	0.9235	1.5207	13
Prime	2009-10	0.2112	0.0161	0	9	4.84	10.31	9.19	10.31	0.9239	0.9722	15
Prime	2010-11	0.1448	0.0163	0.0057	9	4.82	10.34	9.4	10.34	0.8874	0.1766	14
SCBL	2006-07	0.3268	0.0242	0.0183	6	3.81	10.46	9.33	10.46	0.926	0.1032	12
SCB	200	0.32	0.02	0.0	6	3.85	10.	9.4	10.	0.925	0.13	12

L	7-08	85	46	092			52		52	2	87	
SCBL	2008-09	0.3358	0.0253	0.0066	6	3.95	10.61	9.48	10.61	0.9248	0.1792	12
SCBL	2009-10	0.3222	0.027	0.0061	6	4.02	10.6	9.53	10.6	0.9162	0.0983	12
SCBL	2010-11	0.3043	0.0255	0.0062	6	4.07	10.64	9.57	10.64	0.9161	0.0712	12
Sidhartha	2006-07	0.1201	0.012	0.0034	8	4.27	9.9	8.9	9.9	0.9002	0.403	12
Sidhartha	2007-08	0.134	0.0123	0.0069	8	4.27	10.07	9.03	10.07	0.9084	0.5288	12
Sidhartha	2008-09	0.1704	0.0122	0.0045	8	4.57	10.25	9.11	10.25	0.9285	0.4171	12
Sidhartha	2009-10	0.1502	0.0106	0.0053	9	4.31	10.36	9.21	10.36	0.9297	0.2596	20
Sidhartha	2010-11	0.1566	0.0128	0.0079	10	4.31	10.39	9.3	10.39	0.9185	0.3019	12
Sunrise	2007-08	-0.004	-0.005	0	9	0	9.71	8.83	9.71	0.8692	0	12
Sunrise	2008-09	0.0608	0.0051	0	9	0	10.22	9.14	10.22	0.9167	2.4444	12
Sunrise	2009-10	0.1242	0.0121	0.0104	9	4.9	10.23	9.22	10.23	0.9028	0.9859	12
Sunrise	2010-11	0.0206	0	0.0004	9	4.9	10.2	9.33	10.2	0.8646	0.1531	12