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EFFECT OF CORPORATE GOVERNANCE IN FINANCIAL PERFORMANCE OF COMMERCIAL BANKS IN ETHIOPIA

BY

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EFFECT OF CORPORATE GOVERNANCE IN FINANCIAL PERFORMANCE OF BANKING INDUSTRY:

IN THE CASE OF COMMERCIAL BANKS IN ETHIOPIA

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As members of the examining Board of the Final **MBA** open defense, we certify that we have read and evaluated the thesis prepared by Firehiwot Kebede, entitled**:** "**Effect of Corporate Governance in Financial Performance Commercial Banks in Ethiopia"**, and recommend that it be accepted as fulfilling the thesis requirement for the degree of Master of Business administration (Accounting and Finance).

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DECLARATION

First of all, I declare that this thesis is my work and that all sources of the materials used for this thesis have been duly acknowledged. This thesis has been submitted in partial fulfillment of the requirements for MBA degree at Saint Merry University and is deposited at the University library to be made available to users under the rules of the library. I declare that this thesis is not submitted to any other institution anywhere for the award of any academic degree, diploma or certificate.

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ENDORSEMENT

This thesis has been submitted to Saint Mary's University, School of Graduate Studies for examination with my approval as a university advisor.

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Advisor Signature and Date

Table of Contents

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ABBREVATIONS

AIB	Awash International Bank
AUS	Audit committee size
BEQ	Board Educational Qualification
BNKZ	Bank size
BOA	Bank of Abesiniya
BS	Board Size
CBB	Construction and business bank
CBE	Commercial Bank of Ethiopia
CBO	Cooperative Bank of Oromia
CG	Corporate Governance
DB	Dashen Bank
FAG	Firm age
FBM	Frequency of Board meeting
FD	Female Directors
ICGN	International Corporate Governance Network
INSE	Industry specific experience
NBE	National Bank of Ethiopia
NIB	Nib bank
OECD	Organization for Economic Cooperation and Development
ROA	Return on Asset
UB	United Bank
WB	Wegagen Bank

LIST OF TABLES

LIST OF FIGURES

ABSTRACT

This study aims at examining the Effect corporate governance in firms' financial performance using ten years data from the year 2005 to 2014 with a sample of nine Ethiopian commercial banks. The study assessed the relationship between selected corporate governance variables, and bank performance as measured by ROA. Corporate governance variables considered in this study includes board size, board gender diversity, board members educational qualification, industry specific experience, audit committee size and frequency of board meeting. The study controls the effect of bank size and age, of the banks. Explanatory research design was employed to establish the causal relationship between corporate governance and performance measure variables .The study uses both primary and secondary source of data .Primary data was collected using questioner which is completed by board secretary and senior management of the sample commercial banks as they were in better position to comment on corporate governance issues and the secondary data was collected from the National bank of Ethiopia. The study utilizes panel data and fixed effect regression model analysis methodology by using Eviews 7 soft ware in drawing conclusion about the study .The findings of the regression results indicated that large size board and audit committee negatively influences financial performance; whereas board members educational qualification, industry specific experience and board composition positively associated with financial performance. In general, the findings suggest that banks with effective corporate governance mechanisms improve financial performance depending on the measure used even if not all corporate governance mechanisms are significant. Based on the finding and conclusion reached the researcher forwards the following major recommendation attention should be given for the board size of banks to be small in number to optimal level with better educational qualification since small board size with better educational qualification is more effective in monitoring managers and help to improve performance. , boards of banks are dominated by male and board gender diversity is very limited in Ethiopian commercial banks for the last ten years. Thus, there is much to be done to improve the gender balance of boards in Ethiopian banks with a great care about their qualification and competency, Ethiopian commercial banks should include experienced board in other financial sector to improve their financial performance as if the helps the firms to improve their performance by sharing their past experience. Finally, the researcher recommends that Ethiopian commercial banks should make their audit committee size small to improve their performance. Because, as this study revealed large size audit committee negatively influences performance.

Keywords: Corporate Governance, Financial Performance, Commercial Banks and Ethiopia.

CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

Corporate governance refers to generally accepted norms, customs, laws, habits and regulations determining the manner of running the company (Mohan and Marimuthu, 2015). The concept of corporate governance has attracted a good deal of public interest in recent years, because of its apparent importance on the economic health of corporations and society in general. Basically, corporate governance in the banking sector requires judicious and prudent management of resources and the preservation of resources (assets) of the corporate firm; ensuring ethical and professional standards and the pursuit of corporate objectives, it seeks to ensure customer satisfaction, high employee morale and the maintenance of market discipline, which strengthens and stabilizes the bank *(Okoi, Ocheniand John, 2014)*

Corporate governance has become an issue of global significance. The improvement of corporate governance practices is widely recognized as one of the essential elements in strengthening the foundation for the long-term economic performance of countries and corporations (Ibrahim et al., 2010). It has received new urgency because of global financial crisis and major corporate failures that shock major financial centers of the world (Imam and Malik, 2007). Hence, corporate governance has become an important factor in managing organizations in the current global and complex environment.

Melvin and Hirt (2005) described corporate governance as referring to corporate decision-making and control, particularly the structure of the board and its working procedures. The separation of ownership and control in modern corporations leads to an agency problem where the agent operates the firm in line with their own interests, instead of shareholders (Jensen and Meckling, 1976). The need for corporate governance arises from these potential conflicts of interest among stakeholders such as shareholders, board of directors and managers in the corporate structure. According to Imam and Malik (2007) these conflicts of interest often arise from two main reasons. First, different participants have different objectives and preferences.

Second, the participants have imperfect information as to each other's actions, knowledge, and preferences. Corporate governance is intended at reducing divergence of interest and monitoring of controlling interests of the firm, the absence of which firm value is declined (Nanka-Bruce, 2009).

The development has forced national government and regional economic organizations to come up with various guidelines and codes to get businesses to behave decently. One of such institutions is the Organization for Economic Cooperation and Development (OECD), which has undertaken much work on corporate governance for a number of years. Corporate governance arrangements and institutions vary from one country to another. There is no single framework that is appropriate for all countries (*Okoi ,OchenandJohn, 2014).*

The Corporate governance code covers every aspect of the organizational set up, right from how resources are generated and how they are utilized. Therefore, there is need to understand the concepts, processes and problems of corporate governance both from the perspective of those who direct, those concerned with returns and accountability as well as those concern with corporate regulation, because there is a growing consensus that corporate governance has a positive relationship with national growth and development *(Okoi, Ocheniand John, 2014).*

Monetary policy and strategy of a central bank of any country depends on a number of factors that are unique and contextual to that country. Given the policy objective, the strategy, programs depend on the institutional arrangements of formulating and implementing macroeconomic structure of the economy as well as the intensity of involving on international economic and financial activities. During the command economic era, monetary variables were under direct control of the monetary authorities and the banking sector was totally dominated by government banks and private sector was prohibited from entering into the financial sector. As a result, there was only one commercial bank, Commercial Bank of Ethiopia, one construction and saving bank, and one agricultural bank the today's development Bank of Ethiopia (NBE 2009) .

However, since the start of economic reform, following the change of government, the financial sector has undergone reform and the private sector was allowed to invest in the area. Consequently private banks and insurances started to flourish soon after the enactment of a

Monetary and Banking proclamation of 1994. Following these developments attention was shifted from direct control of monetary variables towards market based policy instruments as the government leaves the economy to private sector. As a result of these the central bank could issues different directives, rules, regulations to insure that whether the financial institutions are wisely managed and directed.

Of which corporate governance plays a vital role in maintaining the safety and soundness of financial institution in general and banking sector in particular.

Governance may be said to be all about effective, transparent and accountable administration of affairs of an institution by its management, while protecting the interests of its stakeholders including shareholders, creditors, regulators and the public.

Modern Corporate Governance practices have evolved over time and different codes of best practice on Corporate Governance have been developed by various organizations.

The Basel code of Corporate Governance for banks and financial institutions generally relate to the responsibilities of the Board, Directors, Chairmen, CEOs, senior management, Board appointed committees, auditors, shareholders and regulators. Accountability, internal controls, related party transactions, conflicts of interest, information disclosures have also been extensively dealt with and targeted in the formulation of these principles.

Corporate Governance is also increasingly acknowledged as being an important instrument to address "ownership issues" as well. With the current practices that are available worldwide which can hide the identities of true owners, it is now almost impossible for regulators to only rely on ownership limits to deal with undue influence, or be assured that seemingly unrelated parties are not actually related! Consequently, markets are increasingly looking towards the application of good Corporate Governance practice to overcome any ill-effects that may arise out of ownership concentration and it is generally believed that if good governance is in place, concentrated ownership, known or unknown, may not adversely affect the risk management process of the institution. In the case of banks especially, regulatory limits on ownership in banks are prescribed in a number of countries to prevent banks from being controlled by a single owner or a group of connected owners. In many countries, indirect regulations such as limits on related-party transactions and fit and proper tests for bank directors and executive officers are in place to promote this aspect of good Corporate Governance, and regulators genuinely believe that such practices would increasingly ensure the better risk management of banks, thereby leading to a more sound system.

The Banking and other financial sector is easily distinguishable from the others. The banking business is the key for monetary conditions in a country. Unlike normal business entities which are funded mainly through shareholders' funds; banks' business involves funds raised mainly through deposits. The business of raising public deposits places greater fiduciary responsibilities on the institution and its managers, since depositors' funds need to be safeguarded in a special way, perform as financial intermediaries by lending and investing the funds mobilized and funding economic activities of others are the agents of the payments system where they facilitate payments domestically and internationally, through various instruments such as bank accounts, fund transfers, credit cards etc .These and other activities of the sector undertake as a result of public trust and faith in the stability and soundness of the banks in particular and the system in general because the history on bank failures in many countries indicates that loss of public confidence in banks could be transmittable and could easily lead to banking crisis situations.

In Ethiopia the corporate governance of banks is directed and supervised by the National bank of Ethiopia. The National Bank of Ethiopia monitors and controls the banking business and functions as regulators of the country's money supply and policy institutions. According to banking business Proclamation (No. 592/2008) the national bank is responsible to issue directives on the qualification and competency to be fulfilled by directors; the minimum number of directors in the membership of the board of a bank; the duties, responsibilities and good corporate governance of the boards of directors of bank; the maximum number of years a director may serve in any bank based on this the NBE issued the bank corporate governance directive Number SBB/62/2015 which is enter in to force as of 21st of September,2016.

All in all, as of today, Codes of Best Practice on Corporate Governance set out principles within which values and governance rules should be set by the management of the institution, good Corporate Governance is looked to as being a key tool to be used in the overall risk management of institutions, irrespective of the nature of the business carried out by the institution.

1.2 Statement of the Problem

Effective corporate governance is critical to the proper functioning of the banking sector and the economy as a whole. Banks perform a crucial role in the economy by intermediating funds from savers and depositors to activities that support enterprise and help drive economic growth. Banks' safety and soundness are keys to financial stability, and the manner in which they conduct their business, therefore, is central to economic health. Governance weaknesses at banks that play a significant role in the financial system can result in the transmission of problems across the banking sector and the economy as a whole. Given the importance of corporate governance, several studies have been conducted in developed countries on the relationship between corporate governance and firms' financial performance and found mixed results (see for instance Ayorinde, Toyin and Leye (2012),Bahreini (2013), Kahmarn,Romuald(2009), Giulia R.,Paola F. ,Alessandra R.,(2012), , Punnu(2008),Nazarand Rahim(2015), Inam, AqeelMukhtar (2014) ,Beyene, Srmolo, Kassa.(2013)and Ferede,(2012)) from empirical literature review part of this paper. Most of the prior studies have been undertaken on large firms operating within well organized corporate governance mechanisms in developed economic system. Various governance mechanisms operate differentially for different sizes of firms (Habbash, 2010). Therefore, it is difficult to generalize the same result from the findings of those studies for relatively small size Ethiopian commercial banks governance. Furthermore, Ethiopia's corporate governance landscapes are embedded in a setting that differs from a western context in several ways (DessalegnandMengistu, 2011). Ethiopian banks corporate governance is characterized by the absence of an organized share market and the country has different regulations, practices, and economic features.

Weaknesses in CG arrangements in banks and financial institutions reduce their capacity to identify, monitor and manage their business risk and that can result in poor quality lending and excessive risk-taking by the financial institutions. Depending on the resilience of the financial institutions and markets, these risks have the potential to spread across the wider financial system. Inadequate CG can also lead to a poor credit culture, excessive exposure concentration, poor management of interest risk/exchange risk and inadequacies in the management of connected exposures. Some of these risks, singularly or collectively, can lead to potential insolvency and financial instability

Research studies exclusively on the effect of corporate governance on banks' financial performance are few in developing countries and in Ethiopia it is an unreachable area of research but some studies were conducted in Ethiopia on this area before the NBE issued directives on corporate governance and they also recommend the regulatory body to have this directives. Those studies were undertaken by Fanta ,Kemal ,Waka,(2013)and Fered,(2012),Getahun (2013) were conducted by using only five to seven years data therefore, this study intends to the increase size of the study population and the sample size to the banks and also to increase the number of observations through the use of large sample size and long years data which is not covered by those researchers. The finding of those researchers indicated that board size and existence of audit committee in the board and its size had statistically significant negative effect on bank performance; whereas bank size had statistically significant positive effect on bank performance. Similarly, capital adequacy ratio, as a measure of external corporate governance mechanism, had statistically significant positive effect on bank performance. Whereas, board members educational qualification were positively associated with financial performance. While industry specific experience of director positively related with return on asset but it has a negative effect on net interest margin, the percentage of female directors and board members business management experience does not have a significant effect.

Giving this gap, this study contributes to the existing body of knowledge and bridge the gap by studying the issue with Ethiopian commercial banks. Since banks have a dominant position in developing economic financial systems, and are important engines of economic growth. Since, banking failure would affect the entire financial system and economy.

Keeping this in view and the potential contribution of the banking industry to the economy of developing countries, this study is conducted to examine the Effect of corporate governance on financial performance commercial banks in Ethiopia.

1.3 Objectives of the Study

1.3.1 General Objective of the Study

The main objective of this study is to examine the effect of corporate governance on financial performance commercial banks in Ethiopia.

1.3.2 Specific Objectives of the Study

Given the overall objective of examining the Effect of corporate governance on financial performance commercial banks in Ethiopia, this study had several specific objectives. Specifically, the study wanted to:

- To examine the Effect of board size on financial performance commercial banks in Ethiopia.
- To investigate the effect of board member gender composition on financial performance commercial banks in Ethiopia.
- To identify the influence of board member educational qualification (core competency) on financial performance of commercial banks.
- To identify the effect of board member industry specific experience or tenure in the commercial bank's financial performance.
- To determine the effect of size of audit committee on bank's financial performance
- To identify the effect of Board Meeting frequency on commercial bank's financial performance.
- To identify the change in board structure as a result of the newly implemented corporate governances directive.

1.4. Hypothesis of the study

Various research proposals and writers use research questions. On the other hand, a more formal statement of a research employs hypotheses. These hypotheses are predictions about the outcome of the results to be estimated .Therefore; the study has been tested based on following hypotheses.

Ha- alternative hypothesis

Ha1: There is a negative and significance relationship between board size and commercial banks financial performance.

Ha2 There is a positive and significance attachment between board member gender diversity and commercial banks financial performance.

Ha3: There is a positive and significance association between board members educational qualifications and commercial banks financial performance.

Ha4: There is positive association and significance between board members industry specific experience and commercial banks financial performance

Ha5: There is a negative and significance relationship between size of audit committee and financial performance.

Ha6: there is a negative and significance relationship between frequency of board meeting and commercial banks financial performance.

1.5. Significance of the Study

The result of this study will contribute to commercial bank's firms by identifying relevant corporate governance and how these corporate governance Characteristics affect their financial performance. The result of this study may contribute to the existing literature by providing evidence on the relation between corporate governance characteristics and banks' financial performance and the results would also be the indicators of corporate governance characteristics useful for regulators, managers and business people in making policies and decisions.

1.6. Delimitation of the Study

This study is delimited to examining the effect of internal corporate governance on firms' financial performance by taking evidence from commercial banks in Ethiopia for the period of ten years, from 2005 to 2014. The reason for using this range of period is that the previous studies which was undertaken in Ethiopian related to this topic (Ferede (2012) and Kassa et al(2013))were conducted by using only five and seven years data therefore, this study intends to the increase size of the study population and the sample size to the banks and also to increase the number of observations through the use of large sample size and long years data not covered by those researcher . The dependent variables are delimited to return on asset. The independent variables are delimited to some internal corporate governance characteristics such as board size, board gender composition, directors' educational qualification (core competency), size of audit committee, frequency of board meeting and board members industry specific experience. The study area of this research is delimited to commercial banks in Ethiopia which have available data for the specified period of time.

1.7. Organization of the study

The remaining parts of the paper organized as follows. The second chapter deals with general and empirical literature review related to the topic. The third chapter of the paper describes the materials and methodology part of the paper. In the fourth chapter deals with empirical results and discussion is presented. Finally, in the last chapter ends with the conclusion and recommendation part of the thesis.

CHAPTER TWO

LITERATURE REVIEW

This section have two parts which is the General and empirical literature to analyze and identify the main effect of corporate governance on financial performance of commercial banks.

2.1. General Literature Review

2.1.1. History of Ethiopian Banking Industry

The Ethiopian financial sector is dominated by the banking sector. Banks are the important component of any financial system. They play important role in the economy by transferring fund from the surplus unit to deficit unit of the economy. The efficiency and competitiveness of banking system defines the strength of any economy. Like other developing countries in Ethiopia banks plays a vital role in the process of economic growth and development. The Ethiopian banking sector comprises one development bank, and eighteen commercial banks out of which two commercial banks are state owned including the recently swallowed CBB. The Ethiopian banking system has been regulated with its own key regulatory feature.

According to Mulugeteta, (2010) the key regulatory features were interest rate regulation, credit restrictions, equity market controls and foreign exchange controls.

In Ethiopia the corporate governance of banks is directed and supervised by the central bank. The National Bank of Ethiopia monitors and controls the banking business and functions as regulators of the country's money supply.

According to banking business Proclamation (No. 592/2008) the national bank is responsible to issue directives on the qualification and competency to be fulfilled by directors; the minimum number of directors in the membership of the board of a bank; the duties, responsibilities and good corporate governance of the boards of directors of bank; the maximum number of years a director may serve in any bank.

2.1.2. The Concept of Corporate Governance

Governance is concerned with the manner in which rules and regulations are applied and followed, the relationships that these rules and regulations determine or create and the nature of those relationships (Otieku, 2010). Corporate Governance, therefore, refers to the manner in which the power of a corporation is exercised in the corporation's total portfolio of assets and resources with the objective of maintaining and increasing shareholder value and satisfaction of other stakeholders in the context of its corporate mission (Chenuos, Mohamed, and Bitok, 2014). It is concerned with creating a balance between economic and social goals and between individual and communal goals while encouraging efficient use of resources, accountability in the use of power and as far as possible to align the interests of individuals, corporations and society.

Sound corporate governance encourages the efficient use of resources and provides for accountability for those resources by managers. Institutions that practice good corporate governance are more likely to achieve institutional objectives and goals. Good corporate governance should thus be of prime concern to owners and other stakeholders of the institutions. In fact, good corporate governance helps promote the general welfare of the society and should be of interest to the general public and governments. Corporate Governance broadly refers to the mechanisms, processes and relations by which corporations are controlled and directed.

A governance structure identify the distribution of rights and responsibilities among different participants in the corporation (such as the board of directors, managers, shareholders, creditors, auditors, regulators, and other stakeholders) and includes the rules and procedures for making decisions in corporate affairs. Corporate governance includes the processes through which corporations' objectives are set and pursued in the context of the social, regulatory and market environment. Governance mechanisms include monitoring the actions, policies and decisions of corporations and their agents. Corporate governance practices are affected by attempts to align the interests of stakeholders.

One must note that the key elements of an effective governance structure are ownership (this involves both institutional and managerial), board size, board composition and its structure, CEO characteristics and board members remuneration, auditing, information, and the market for corporate control (Keasey et al 1997 as cited on Vishwakarma, 2015)

2.1.3 Corporate Governance Mechanisms and Firms' Financial Performance

Adopting better corporate governance mechanisms such as an enhanced board and audit committee improves monitoring of management and reduces information asymmetry problems (Aldamen et al., 2011). There is a significant literature that links size, gender diversity, and other characteristics of the board of directors and audit committees to improved firm performance (Klein, 1998; Aldamen et al, 2011).Corporate governance mechanisms have been identified as an essential tools needed in managing any corporation including banks. There are different mechanisms that reduce agency cost whereby corporate governance can be measured in an organization. In the corporate governance literature board characteristics (board size, board gender diversity and educational qualification and experience) and audit committee size were used as corporate governance mechanisms.

International organizations such as Organization for Economic Cooperation and Development (OECD) and International Corporate Governance Network (ICGN) have developed corporate governance principles which stressed on the role of boards.

According to Bathula (2008), corporate governance principles focus on the importance of corporate governance for long-term economic performance and strengthening of international financial system. A strong board can play a decisive role in improving firm financial performance. The important role of boards is to act as an internal governance mechanisms and monitoring of management (Shleifer and Vishny, 1997). An effective board is likely to help the firm achieve better performance by effectively under taking their monitoring duties (Bathula, 2008). Board of directors is an important corporate governance mechanism (Aljifriand Moustafa,2007). Boards of directors are the agent of the shareholders and their primary task is to monitor and control firm management on behalf of shareholders to reduce agency problem.

In Modern Corporation's board of directors are charged with the task of monitoring the activities of top management to ensure that the managers act in the best interests of shareholders (Jensen and Meckling, 1976). From the agency theory point of view boards have play decisive role in alleviating agency problems that arising from the separation of ownership and control of firms (O'Connell and Cramer, 2010). In doing so the board of directors need to be effectively supervise the activities of top management. The effectiveness of the board is influenced by factors such as board composition and quality, size of board, , board diversity, board committee effectiveness such as audit committee and information asymmetries ultimately this affects the board oversight performance (Uadiale, 2010). When the board is effective it is expected to drive the company towards better financial achievement (Andres and Vallelado, 2008). When financial markets are not well developed as an efficient external control mechanism and when the shareholders are not well protected due to weak legal system and poor law enforcement the role of the board of director becomes highly significant as an internal control mechanism (Gonz´alez and Garay, 2003). Boards of director are the heart of corporate governance. However, the effectiveness of the board of directors as shareholders' monitoring mechanism can only be efficient if bounded with appropriate size, composition and sub-committee (Lawal, 2012).

The audit committee is a sub-committee of the board of directors and its primary role is to monitor and review financial statements (Yammeesri and Herath, 2010). An audit committee has a particular role of ensuring that the interests of shareholders are properly protected in relation to financial reporting and internal control (Habbash, 2010). The use of an audit committee is an important part of the decision control system for internal monitoring by boards of directors (Famaand Jensen, 1983). Monitoring is performed by external audit and audit committees. The existence of an audit committee improves the monitoring of corporate financial reporting and internal control and it helps to promote good corporate governance in turn this improves firms' financial performance by reducing agency cost (Al –Sa'eed and Al-Mahamid, 2011). Size is vital characteristics of audit committees (Habbash, 2010).

2.1.3.1 Board Size

According to Kiel and Nicholson (2003) board size is crucial to achieving the board effectiveness and improved firm performance. According to Lawal (2012), board size affects the quality of deliberation among members and ability of board to arrived at an optimal corporate decisions. Therefore, identifying the appropriate board size is essential because size can be detrimental to corporate governance effectiveness beyond optimal level. However, determining an ideal size of the board has being an ongoing and controversial debate in corporate governance literature (Lawal, 2012). Whether large or small board help improve firm performance it is debatable issue and researcher's found mixed result about the relation between board size and firm performance. Jensen (1993) argues that a larger board leads to less effective monitoring due to coordination and process problems inherent in large board size. Larger boards can be less participative, less cohesive, and less able to reach consensus. Coordination, communication and decision-making problems increasingly impede company performance when the number of directors increases (Yermack, 1996 as cited by Uadiale,2010).

Al-Manaseer et al. (2012) also argues that boards with too many members lead to problems of coordination in decision making. Small board size was favored to promote critical, genuine and intellectual deliberation and involvement among members which presumably might led to effective corporate decision making, monitoring and improved performance (Lawal, 2012). In contrast Klein (2002) suggested that larger boards able to promote effective monitoring due to their ability to distribute the work load over a greater number of observers. Thus, board size can influence the financial performance of firms.

2.1.3.2 Board Gender Diversity

Gender diversity is part of the broader concept of board diversity. Boards are concerned with having right composition to provide diverse perspectives. Greater female representation on boards provides some additional skills and perspectives that may not be possible with all-male boards (Boyle and Jane, 2011). Board diversity promotes more effective monitoring and problem-solving. He suggests that female board members will bring diverse viewpoints to the boardroom and will provoke lively boardroom discussions. Gender diversity in the boards is supported by different theoretical perspectives. Agency theory is mainly concerned about monitoring role of directors. Representation from diverse groups will provide a balanced board so that no individual or group of individuals can dominate the decision-making of the board (Erhardt et al., 2003). The management may be less able to manipulate a more heterogeneous board to achieve their personal interests. Gender diversity is associated with effectiveness in the oversight function of boards of directors. The oversight function may be more effective if there is gender diversity in board which allows for a broader range of opinions to be considered.

According to Erhardt et al. (2003), diversity of the board of directors and the subsequent conflict that is considered to commonly occur with diverse group dynamics is likely to have a positive impact on the controlling function and could be one of several tools used to minimize potential agency issues. From stakeholders' theory, diversity also provides representation for different stakeholders of the firm for equity and fairness (Keasey et al., 1997). From resource dependency perspective, the board is a strategic resource, which provides a linkage to various external resources (Walt and Ingley, 2003). This is facilitated by board diversity. On the other hand, Rose (2007) revealed insignificant association between number of women directors on the board and firm performance. However, many scholars now believe that an increase in board diversity leads to better boards and governance on the ground that diversity allows boards to tap on broader talent pools for the role of directors (Bathula, 2008). However, as he stated in corporate world women representation on boards is very limited.

2.1.3.3 Educational Qualification

Director's educational qualifications are central to effectively interpret and utilize the information generated by the management of particular types of business enterprise. Educational qualification is potentially important since the ability to seek and interpret appropriate information is essential for the efficient operation of the modern corporation and the effective control or guidance of management by boards of directors. Educational qualification affects the oversight and monitoring role of boards of directors (Gantenbein and Volonte, 2011).Board of directors is vested with the responsibility of ensuring that the shareholders’ money is not wasted, shareholders have a serious interest in ensuring that the board is staffed with well educated and experienced directors (Gantenbein and Volonte, 2011). The human capital provided by its board of directors is vital given the corporate board is one of the mechanisms for overseeing the firm and it can arguably provide the knowledge needed to function in the new environment. Personal profile factors of directors such as education and experience is important for board efficiency.

2.1.3.4 Industry Specific Experience

Appointing directors with related and relevant skills and knowledge to perform task specific duties such as the firm's internal control and procedures will enhance the quality of information gathered and the solution to problems and of the views held and judgments made during the decision-making process (DeZoort, 1998 as cited by Saat, et al, 2011). Directors' specialist knowledge will be valuable to the creation of a strong and informed board (Saat et al., 2011). He claimed that experience of directors enables them to guide, steer and monitor the firm more effectively. In other words, their knowledge of the industry, its opportunities and threats and their connections to the industry participants based on their experience enables them to contribute substantively in the firm performance.

2.1.3.5 Audit Committee Size

An audit committee is an operating committee of the board of directors charged with oversight of financial reporting and disclosure. Committee members are drawn from members of the company's board of directors, with a Chairperson selected from among the committee members. Its role includes choice and monitoring of accounting principles and policies, overseeing appointment, dismissal of external auditors, monitoring internal control process, discussing risk management policies and practice with management and overseeing the performance of internal audit function.

According to Jensen and Meckling (1976) the audit committee plays a significant role in the monitoring process carried out by the directors of the firm and auditing is used by firms to reduce agency costs. In addition to that they revealed that most essential board decisions originate at the committee level, and this includes the audit committee. Audit committees thus, represent another internal governance mechanism whose impact is to improve the quality of financial management of a company and hence its performance.

Kyereboah-Coleman (2007) reported a significant positive relation between size of the audit committee and firm performance (ROA and Tobin’s q) using the overall sample. Kyereboah-Coleman (2007) describe that size of the audit committee could be an indication of the seriousness attached to issues of transparency by the organization. However, only using Ghanaian sample the size of the audit committee showed a negative effect on performance. He explained as free-ridership and difficulty in consensus building in large groups leads to low performance. In addition, Lin et al (2006) found significant positive association between audit committee size and occurrence of earnings restatement. It was explained that a certain minimum number of audit committee members may be relevant to the quality of financial reporting.

Aldamen et al. (2011) reveals that smaller audit committees with more experience and better educational qualifications are more likely to be associated with positive firm performance. In Ethiopia banking industry, Ferede (2012) found that large number of audit committee has a negative and significant effect on financial performance. He added that Limiting audit committee size to reasonable number improves audit committee effectiveness. Thus, it is expected that there is a Negative relationship between size of audit committee and financial performance.

2.1.3.6. Meeting Frequency of Board

Meeting frequency refers to how much time Board meet on a year. For board to effectively perform its oversight function and monitor management performance, the board must hold a regular meeting. Measuring the intensity and effectiveness of corporate monitoring and discharging is the frequency of board meetings (Jensen M. , 1993). Empirical findings on the effect of frequent board meetings and corporate performance show mixed results. Some studies concluded more meeting frequency has a negative impact on the performance of firms. Meeting Frequency has a significant negative impact on ROA and an increasing in meeting frequency will reduce the ROA (Ms.S.DanoshanaandMs.T.Ravivathani, 2013). Moreover, Akpan (2015) found that board meetings negatively and significantly relate with company performance. Another study conducted on public listed companies in Malaysia using five years data 2003 to 2007 of 328 companies, shows that the higher the number of meetings the worse the firm performance (Amran, 2011). Whereas, Karamanou et al (2005) found a positive association between frequency board meeting and management earnings forecasts, using a sample of 157 firms in Zimbabwe from 2001-2003; Mangena and Tauringana (2008) report a positive relationship between board meeting frequency and corporate performance. Similarly in a study of the sample of 169 listed corporations from 2002-2007 in South African, a statistical significant and positive association between the frequency of board meeting and corporate performance exist (Ntim and Osei, June 2011). This implies that the board of directors in South Africa that meet more frequently tend to generate higher financial performance. Moreover, Ntim and Osei (2011) found a statistically significant and positive association between the frequency of corporate board meetings and corporate performance, implying that South Africa boards that meet more frequently tend to generate higher financial performance.

2.1.4 Theoretical Framework of the Study

Corporate governance is the relationship among shareholders, board of directors and the top management in determining the direction and performance of the corporation. It includes the relationship among the many players involved (the stakeholders) and the goals for which the corporation is governed (Kim and Rasiah, 2010). According to Imam and Malik (2007) the corporate governance theoretical framework is the widest control mechanism of corporate factors to support the efficient use of corporate resources. The challenge of corporate governance could help to align the interests of individuals, corporations and society through a fundamental ethical basis and it fulfills the long term strategic goal of the owners. It will certainly not be the same for all organizations, but will take into account the expectations of all the key stakeholders (Imam and Malik, 2007). So maintaining proper compliance with all the applicable legal and regulatory requirements under which the company is carrying out its activities is also achieved by good practice of corporate governance mechanisms. There are five major theoretical frameworks that can be identified from the corporate governance literature: agency, stewardship, resource dependence, stakeholder and managerial-hegemony. These theories have evolved from many disciplines such as finance, economics, law, management and organizational behavior. For instance, agency theory arises from the field of finance and economics and stakeholder theory from a more social-oriented perspective on corporate governance. All these disciplines have contributed to the development of theoretical aspects of corporate governance.

There are a number of theoretical perspectives which are used in explaining the Effect of corporate governance on firms' financial performance. The most important theories are the agency theory, stakeholders' theory and resource dependency theory (Maher andAndersson, 1999).These theories are discussed as follows.

2.1.4.1 Agency Theory

The existence of divergent and sometimes conflicting objectives between managers and shareholders has given rise to the design of many concepts and mechanisms to ensure that the cost associated with such divergent interest is minimal. One of the proposed arrangements is corporate governance and it is not surprising that agency theory has been the dominant paradigm in the corporate governance literature (Coleman,2007).

Agency theory is widely used as a means of explaining various corporate governance issues. According to Habbash (2010) agency theory is the most popular and has received greater attention from academics and practitioners. The agency theory is based on the principal agent relationships. The separation of ownership from management in modern corporations provides the context for the functioning of the agency theory. In modern corporations the shareholders (principals) are widely dispersed and they are not normally involved in the day to day operations and management of their companies rather they hire mangers (agent) to manage the corporation on behalf of them (Habbash, 2010). The agents are appointed to manage the day to day operations of the corporation. The separation of ownership and controlling rights results conflicts of interest between agent and principal. To solve this problem or to align the conflicting interests of managers and owners the company incurs controlling costs including incentives given for managers. According to Bowrin and Navissi (n.d.) as sited by Ferede(2012) agency theory refers to a set of propositions in governing a modern corporation which is typically characterized by large number of shareholders who allow agents to control and manage their collective capital for future returns. The agent, typically, may not always own shares but may possess relevant professional skills and competence in managing the corporation. The theory offers many useful ways to examine the relationship between owners and managers and verify how the final objective of maximizing the returns to the owners is achieved, particularly when the managers do not own the corporation's resources. Agency theory identifies the role of the monitoring mechanism of corporate governance to decrease agency costs and the conflict of interest between managers and owners. It is clear that the principal-agent theory is generally considered as the starting point for any debate on the issue of corporate governance. Agency theory having its roots in economic theory was exposited by Alchian and Demsetz (1972) and further developed by Jensen and Meckling (1976) as cited by Ferede ,(2012).

Jensen and Meckling (1976) defined agency relationship as a contract under which the principal engage another person or the agent to perform some service on their behalf which involves delegating some decision making authority to the agent. If both parties to the relationship are utility maximizes, there is good reason to believe that the agent will not always act in the best interests of the principal. The principal can limit divergences from his interest by establishing appropriate incentives for the agent and by incurring monitoring costs designed to limit the irregular activities of the agent.

According to agency theory the agent strive to achieve his personal goals at the expense of the principal. Mangers are mostly motivated by their own personal interests and benefits, and work to maximize their own personal benefit rather than considering shareholders interests and maximizing shareholders wealth. To reduce agency problem there must be better monitoring and controlling mechanisms which helps to ensure that managers pursue the interests of shareholders rather than only their own interests *agency costs (Bathula, 2008,).* The concept of corporate governance presumes a fundamental tension between shareholders and corporate managers (Jensen and Meckling, 1976). While the objective of a corporation's shareholders is a return on their investment, managers are likely to have other goals, such as the power and prestige of running a large and powerful organization, or entertainment and other perquisites of their position. Managers' superior access to inside information and the relatively powerless position of the numerous and dispersed shareholders, mean that managers are likely to have the upper hand (Fama and Jensen,1983).Therefore, shareholders monitor and controls managers through their representatives such as board of directors. Boards of directors are considered as an important device to protect shareholders from being exploited by managers and help to effectively control managers when they try to maximize their self interest at the expense of the company's profitability. Fama and Jensen (1983) argues that in order to minimize agency problem that emanates from the separation of ownership and control the corporations need to have a mechanisms that enables to separate the authority of decision management from decision control. This would reduce agency costs and ensures maximization of shareholders wealth by effectively controlling the power and self-centered decisions of management.

The agency theory provides a basis for the governance of firms through various internal and external mechanisms. Corporate governance mechanisms are designed to align the interest of owners and managers, constrained the opportunistic behaviors of managers and protect shareholder interests, generally to solve agency problem (Habbash, 2010). Corporate governance is a mechanism through which shareholders are assured that managers will act in their best interests and it limits agency problems. Agency theory suggests that there are a number of mechanisms to reduce the agency problem in the company such as choosing appropriate board composition (in terms of size, gender, experience and competence), effective audit committee, and the threat of firing (Tandelilin et al., 2007). From agency theory view point, corporate governance improves corporate performance by resolving agency problems through monitoring management activities, controlling self-centered behaviors of management and inspecting the financial reporting process (Habbash, 2010). Moreover, corporate governance is able to alleviate agency costs by aligning the conflicting interests of management and shareholders through monitoring management and using different corporate governance mechanisms. Therefore, corporate governance mechanism such as boards of directors and audit committees enables shareholders to closely monitor the activities of managers. Ineffective board and audit committee may give confidence for managers to pursue their own interests but effective board and audit committee can reduce deceptive behavior of managers by detecting fraudulent financial report and actively monitoring.

According to the assumptions of agency theory corporate governance mechanisms affect financial performance. As a consequence, enhancing corporate governance mechanisms should result in improved financial performance. Taking agency theory into consideration, the study variables were identified with the aim of examining the relationships between corporate governance characteristics and financial performance. Board structure has relied heavily on the concepts of agency theory, focusing on the controlling function of the board (Habbash, 2010). The corporate governance mechanisms considered in this research include board size, board gender diversity, educational qualification of board members, industry specific experience of board members frequency of meeting and audit committee size.

2.1.4.2 Stakeholders Theory

Stakeholder theory is an extension of the agency theory, where the agency theory expects board of directors to protect only the interests of shareholders. However, stakeholder theory extends the narrow focus of agency theory on shareholders interest to stakeholders to take into account the interests of many different groups and individuals, including interest groups related to social, environmental and ethical considerations (Freeman et al., 2004).

According to Freeman et al. (2004), stakeholder theory begins with the assumption that values are necessarily and explicitly a part of doing business. It asks managers to articulate the shared sense of the value they create, and what brings its core stakeholders together. It also pushes managers to be clear about how they want to do business, specifically what kinds of relationships they want and need to create with their stakeholders to deliver on their purpose. According to stakeholder theory the purpose of the firm is to serve and coordinate the interests of its various stakeholders such as shareholders, employees, creditors, customers, suppliers, government, and the community.

According to Habbash (2010), stakeholder refers to any one whose goals have direct or indirect connections with the firm and influenced by a firm or who exert influence on the firms goal achievement. These include management, employees, clients, suppliers, government, political parties and local community.

According to this theory, the stakeholders in corporate governance can create a favorable external environment which is conducive to the realization of corporate social responsibility. Moreover, the stakeholders in corporate governance will enable the company to consider more about the customers, the community and social organizations and can create a stable environment for long term development. The benefit of the stakeholder model emphasis on overcoming problems of underinvestment associated with opportunistic behavior and in encouraging active co-operation amongst stakeholders to ensure the long-term profitability of the business firm (Maher and Andersson, 1999) .According to Coleman (2007) management receive capital from shareholders, they depend upon employees to accomplish the objective of the company. External stakeholders such as customers, suppliers, and the community are equally important, and also constrained by formal and informal rules that business must respect. According to stakeholders theory the best firms are ones with committed suppliers, customers, and employees and management. Recently, stakeholder theory has received attention than earlier because researchers have recognized that the activities of a corporate entity impact on the external environment requiring accountability of the organization to a wider audience than simply its shareholders (Coleman, 2007). Companies are no longer the instrument of shareholders alone but exist within society. It has responsibilities to the stakeholders. However, most researchers argue that it is unrealistic task for managers (Sundaram and Inkpen, 2004b; Sanda et al., 2005). The stakeholder theory has not been subjected to much empirical study. The common criticisms for stakeholder theory is that how to align the stakeholders conflicting interests since the difficulties result from how to administer different stakeholders with various needs and demands. It is not possible to treat all stakeholders equally (Habbash, 2010). Moreover, it is not practical for all stakeholders to be effectively represented in corporate governance recommendations as this may undermine the welfare of company (Habbash, 2010). The other critique of the stakeholder model is that managers or directors may use "stakeholder" reasons to justify poor company performance (Maher and Andersson, 1999).

2.1.4.3 Stewardship Theory

According to the stewardship theory, a manager's objective is primarily to maximize the firm's performance because a manager's need of achievement and success are satisfied when the firm is performing well. One key distinguishing feature of the theory of stewardship is that it replaces the lack of trust to which agency theory refers with respect for authority and inclination to ethical behavior (Coleman, 2007).

2.1.4.4. Resource Dependency Theory

This theory introduces accessibility to resources, in addition to the separation of ownership and control, as a critical dimension to the debate on corporate governance. Again, the theory points out those organizations usually tend to reduce the uncertainty of external influences by ensuring that resources are available for their survival and development. By implication, this theory seems to suggest that the issue of dichotomy between executive and non-executive directors is actually irrelevant. How then does a firm operate efficiently? To resolve this problem, the theory indicates that what is relevant is the firm's presence on the boards of directors of other organizations to establish relationships in order to have access to resources in the form of information which could then be utilized to the firm's advantage. Hence, this theory shows that the strength of a corporate organization lies in the amount of relevant information it has at its disposal (Coleman, 2007).

At the same time as the stakeholder theory focuses on relationships with many groups for individual benefits, resource dependency theory concentrates on the role of board directors in providing access to resources needed by the firm (Abdullah and Valentine, 2009). According to this theory the primary function of the board of directors is to provide resources to the firm. Directors are viewed as an important resource to the firm. When directors are considered as resource providers, various dimensions of director diversity clearly become important such as gender, experience, qualification and the like. According to Abdullah and Valentine, directors bring resources to the firm, such as information, skills, business expertise, access to key constituents such as suppliers, buyers, public policy makers, social groups as well as legitimacy. Boards of directors provide expertise, skills, information and potential linkage with environment for firms (Ayuso and Argandona, 2007). The resource based approach notes that the board of directors could support the management in areas where in-firm knowledge is limited or lacking. The resource dependence model suggests that the board of directors could be used as a mechanism to form links with the external environment in order to support the management in the achievement of organizational goals (Wang, 2009). The agency theory concentrated on the monitoring and controlling role of board of directors whereas the resource dependency theory focus on the advisory and counseling role of directors to a firm management. Recently, both economists and management scholars tend to assign to boards the dual role of monitors and advisers of management. However, whether boards perform such functions effectively is still a controversial issue (Ferreira, 2010). Within a corporate governance framework, the composition of corporate boards is crucial to aligning the interest of management and shareholders, to providing information for monitoring and counseling, and to ensuring effective decision-making (Marinova et al., 2010). The dual role of boards is recognized. However, board structure has relied heavily on agency theory concepts, focusing on the control function of the board (Habbash, 2010). Each of the above theories is useful in considering the efficiency and effectiveness of the monitoring and control functions of corporate governance. But, many of these theoretical perspectives are intended as complements to, not substitutes for, agency theory (Habbash, 2010).

Among the theories discussed, agency theory is the most popular and has received the most attention from academics and practitioners. According to Habbash (2010), the influence of agency theory has been instrumental in the development of corporate governance standards, principles and codes. Mallin (2007) provides a comprehensive discussion of corporate governance theories and argues that the agency approach is the most appropriate because it provides a better explanation for corporate governance roles (Habash, 2010).

This study is therefore, will draw on agency theory to test whether hypothesized relationships exist between corporate governance and firms' financial performance. The agency theory framework has the ability to explain internal corporate governance. It can also explain the expected association between corporate governance mechanisms and financial performance.

2.2. Review of Previous Empirical Studies

This section of literature review concentrates on previous studies that have been conducted in relation to the area of study. Different researchers have studied the Effect of corporate governance on firm's performance from different perspectives in different environments using a number of variables of interest and mixed results were concluded by previous studies in relation to the relationship between corporate governance and firms’ financial performance. The empirical studies are summarized below in this section.

2.2.1 Empirical Evidence in the World

The study undertaken by (Bahreini , 2013) provides the direction that the corporate governance characteristics specially board of directors and audit committee on performance of banks in Malaysia. According to the study the relationship between the variables were tested by using five years(2005-2009) annual report and analyzed by using descriptive statistics and regression analysis tools .The main finding of this paper is that out of the six corporate governance characteristics used in the hypothesis testing or the model board size, audit committee size and audit committee meeting have positive relationship between and the other (percentage of independent non executive board of directors and percentage of independent non executive audit committee members have negative correlation with firm performance

(Return on equity and Tobin's Q) and the result for the percentage of independent board of directors member is not significant .

Bathula (2008) studied the association between board characteristics and firm performance. Board characteristics which were considered in the research include board size, director ownership, chief executive officer duality, gender diversity, educational qualification of board members and number of board meetings. Additionally, firm age and firm size was used as control variables. Firm performance was measured by return on assets. To test the hypothesis a sample of 156 firms over a four year period data from 2004 to 2007 was used. The sample includes all firms listed on New Zealand stock exchange. Empirical analysis was undertaken using Generalized Least Squares analyses. The findings of the study showed that board characteristics such as board size, chief executive officer duality and gender diversity were positively related with firm performance, whereas director ownership, board meetings and the number of board members with PhD level education was found to be negatively related. Firm age and firm size does not have significant influence.

The study by (Marn and Romuald, 2009) they investigate the relationship between corporate governance and company performance using panel data from 20 public listed companies in Malaysia.

The required information was collected from 100 annual reports from 20 Malaysian companies. Panel data was utilized and the data gathered were analyzed using descriptive statistics, correlation, and regression. Five main corporate governance variables were analyzed in terms of their relative impact on corporate performance (Earnings per Share (EPS) and the independent variables employed in this study were board size, board composition, audit committee, CEO status and Ownership structure. Based on the results of the study, it has been observed that both Board Size and Ownership structure variables have a significant effect on firm performance The remaining three other hypotheses did not show any significance. Board composed by higher proportion of independent non-executive directors does not have any effect on the corporate performance. The results also show that a majority of independent non-executive directors in the audit committee does not have any significant influence the firm performance.

Mahan and Marimuthu ,(2015) on their study on the relationship between corporate governance on selected Indian companies . On this study the researcher employed one dependent variable (ROA) and five independent variable i.e board size, CEO duality, remuneration to board of directors, independent directors and board ownership. The researcher uses SPSS, correlation, regression and means to analyze the collected data. The finding indicates that size of board, remuneration to directors and composition of independent directors in the board do not have any sort of impact on the financial performance of firms listed in the Bombay Stock exchange, the two corporate governance variables of board ownership and duality are exerting significant impact on financial performance ,presence of promoters in the board is the single corporate governance variable which shall significantly enhance financial performance of a firm.

Punnu.,(2008) analyze the relationship between governance structures and firm performance particularly board structure and CEO duality, on the performance of Malaysian public listed companies. Using samples of large publicly traded Malaysian companies, this research aims to examine the relationship between CEO duality and the proportion of independent directors on firm performance as measured by return on assets (ROA) and return on equity(ROE).the result of the study was analyzed by SPSS and other supporting tools. Results show that there is no significant relationship between corporate governance structures and company performance.

Nazar, Rahim(2015) analyze the impact corporate board size and corporate performances of Sri Lankan listed companies by employing a cross sectional analysis of 109 firms listed in Colombo Stock Exchange(CSE) for the financial year ending 2013 and multivariate analyses are used to test the hypotheses. The independent ,dependent and control variables used in this study were board size, ROA and ROE and board independence, CEO duality, leverage, firm size and dividend yield respectively. The results show that board size is significantly negatively associated with ROA and insignificantly negatively linked with ROE. Control variables of board independent, CEO duality and leverage are negatively related with ROA and ROE.

Giulia R., Paola F., and Alessandra R., (2012) provided evidence on the interaction between corporate governance and performance in the Italian banking groups during the period 2006-

2010 by Using the fixed effect model on a panel data set and the sample consists of the sample consists of 25 Italian banking and the researcher uses seven independent variables (board size, board composition, existence of board committees, control and risk (audit) committee size and membership, board remuneration, and women directorship) and two depended variables (ROA and ROE) to test the interaction between corporate governance and firm performance. The date was analyzed by using descriptive and regression analysis tools.

The finding of this paper is that board size does not affect Italian bank holding companies' performance and that smaller audit committees charged with internal control activities perform better, a significant negative relationship between the percentage of independent directors in the audit committee and banks' performance in terms of both ROE and ROA. The study also shows also a significant positive relationship between the presence of women on the board of directors and both ROE and ROA. The other dimensions of corporate governance (board independence, board committees' existence, audit committee size, and board remuneration) do not have a statistically significant relationship with bank groups' profitability.

Ibrahim et al. (2010) examined the role of corporate governance in firm performance. His study was a comparative analysis between chemical and pharmaceutical sectors of Pakistan using a sample of five companies from each sector from the year 2005 to 2009. Multiple linear regression models with panel data methodology were used. Return on asset and return on equity was used as a measure of performance and they used three corporate governance variables; board size, board independence and ownership concentration. They found that in both sectors, the impact of corporate governance on return on equity is significant but there is no significant impact on return on asset. In case of sector analysis, there is an insignificant impact of corporate governance on return on asset for chemical and pharmaceutical. On the other hand, there is a significant impact of corporate governance on return on equity in chemical sector, but in pharmaceutical the impact is insignificant.

Amran (2011) empirically studied the association between Corporate Governance Mechanisms and Company Performances. It was expected that corporate governance mechanisms affect company performance. The hypothesis was tested on 424 public listed Malaysian Companies (233 family controlled firms and 191 non-family controlled firms) and the data about corporate governance mechanisms and company's performance was collected from Sultanah Bahiyah Library database from the year 2003 to 2007. The independent variables used in this study were Board size, board independence director's professional qualification, leadership structure the control variables include debt, firm age and firm size and Tobin's Q were used as a measure of company performance. Panel data methodology with generalized least square estimation method was used to test the hypothesis. The analysis has been done by classifying the sample as family controlled firm and non-family controlled firm. The researcher revealed that director's qualification measured as the percentage of directors with degree and above divided by total directors helps to enhance the performance of non-family controlled firms but insignificant for family controlled firms. Board size and leadership duality was a significant negative influence on family controlled firms performance but insignificant for non-family controlled firms. Firm age was a significant negative and positive association between the performance of family controlled and non-family controlled firms respectively. On the other hand, there was a significant negative relationship between firm size and performance of both family controlled and non-family controlled firms. The other variables such as board independence and director's professional qualification were insignificant for both classes of firms.

HifzaI.and Aqeel M.(2014), provide the evidence on the impact of corporate governance on Pakistan banking sector .Performance of banking sector is measured through liquidity, profitability, growth, asset quality, operational efficiency, privatization, investor's protection, disclosure; cost of equity; capital adequacy indicator and expense management and the non of the corporate governance mechanism were indicated on the study . This study has been conducted over commercial banks of Pakistan. The empirical results show that there is strong association of corporate governance and determinants of banking sector performance. Results of this study show that banks with good corporate governance show better performance as compared to banks having less corporate governance.

Al -Manaseer et al. (2012) empirically investigated the impact of corporate governance on performance using 15 Jordanian banks listed at Amman Stock Exchange from the year 2007 to 2009 with a total of 45 bank-year observations. The study employed pooled data, and OLS estimation method with panel methodology. Return on asset, return on equity, profit margin and earnings per share were the dependent variables of the study and board size, board composition (independence), chief executive officer status, foreign ownership and bank size were the independent variables of the study. The study revealed a significant negative relation between board size and banks performance as measured by return on equity and earnings per share but insignificant negative association of board size with return on asset and profit margin was found. Bank size was negatively related with return on asset, return on equity and profit margin but only significant with profit margin. The study also reveals a positive association between board composition and foreign ownership and bank performance. In addition, chief executive officer status has a negative influence.

The study by Khaled A., and Mohamed K., (2007) provided evidence on the impact of corporate governance mechanisms on firms' performance using 51 United Arab Emirates listed firms by using both accounting and market data for the year 2004. They employed cross-sectional regression analysis to test whether the selected corporate governance variables have an impact on firms' performance or not after controlling firm size. The finding of the study showed that the governmental ownership, the debt ratio, and the payout dividends ratio have a significant impact on the firm performance (Tobin's Q); whereas the institutional investors, the board size, the firm size, and the audit type have insignificant effect on firms' performance. The study was concluded that three of the corporate governance mechanisms; governmental ownership, debt ratio, and the payout dividends ratio were strong enough to affect the performance of United Arab Emirates listed firms.

2.2.2 Empirical Evidence in Africa

Studies have been conducted on effect of corporate governance on the financial performance of firms in Africa which including research made in Rwanda, Nigeria, Libya, Kenya,Ghana. According to Xavier, Shukla, Oduor, Mbabazize (2015) the study on the effect of corporate governance on Financial Performance of commercial banks in Rwanda. The study has four objectives which determined how board size, CEO duality, institutional ownership, board composition affect financial performance of commercial banks in Rwanda. The researcher used a descriptive research design in analyzing the effect of corporate governance and financial performance of commercial banks in Rwanda, this study made use of primary and secondary data. The study collect primary data concerning corporate governance through open ended and closed questions that has been distributed to the sample size and data drawn from the annual reports of the banks under review. The study has been based on the four independent variables which are CEO duality, board composition, board size as well as institutional ownership. Financial Performance was measured by the Return on Assets and return on equity of each commercial bank. The finding of the study shows that board size and CEO duality have no effect on performance of commercial banks in Rwanda, Board composition had a negative effect and it was found that institutional ownership was not a significant factor in explaining profitability.

The same study which was undertaken by Ayorinde, Toyin, Leye (2012) on examined the effects of corporate governance on the performance of Nigerian banking sector by using secondary source of data which was sought from published annual reports of the quoted banks for the period of five years 2006-2010 by employing Person Correlation and the regression analysis to test the relationship between the corporate governance variables(board size, directors equity interest and CG discloser index) and firms performance (ROA and ROE). The study discovered that a negative but significant relationship exists between board size and the financial performance of these banks while a positive and significant relationship was also observed between directors' equity interest and level of corporate governance disclosure index and performance of the sampled banks.

Pun (2015) on his study on the effect of board committees on corporate financial performance among companies listed on the Ghana Stock Exchange (GSE) and he found board committees had no statistical significant effect on the corporate financial performance of listed firms. Specifically, nomination committee regressed negatively on corporate financial performance but was statistically insignificant, audit committee have no effect whiles remuneration committee predicted positively but also not statistically significant on corporate financial performance .The quantitative research approach was adopted to study the prognostic effect of board committee on corporate financial performance for companies consistently listed on the GSE from 2006-2010. Data was sourced from annual reports of listed companies and a static panel regression model was employed to analyze the presence of various committees on corporate financial performance.

Mohammed,(2011)on his study on the topic of the impact of corporate governance on the performance of banks in Nigeria by using both primary and secondary data and concludes that corporate governance significantly contributes to positive performance in the banking sector. The secondary data obtained from the annual financial statement of the banks for a period of five accounting year used in analyzing the financial ratios for the study and questionnaires were distributed to the staff of the selected banks. The primary data was analyzed through inferential statistical the chi-square analysis method. The secondary data collected from the audited annual reports of the banks were subjected to descriptive statistical analysis through data tabulation. The non-probability sampling technique was used for this study.The ratios employed in this study includes Return on capital, Current ratio, Debt ratio, Dividend cover and Retention ratio.

The study by Uadiale (2010) examining the impact of board structure on corporate financial performance in Nigeria. He found that the existence of strong positive association between board size and corporate financial performance. It investigates the composition of boards of directors in Nigerian firms and analyses whether board structure has an impact on financial performance, as measured by return on equity and return on capital employed. Based on the extensive literature, four board characteristics (board composition, board size, board ownership and CEO duality) have been identified as possibly having an impact on corporate financial performance and these characteristics are set as the independent variables. The Ordinary Least Squares (OLS) regression was used to estimate the relationship between corporate performance measures and the independent variables. Further he noted as exists of positive association between outside directors sitting on the board and corporate financial performance. However, a negative association was observed between directors' stockholding and firm financial performance measures. In addition, the study reveals a negative association between return on capital employed (ROE) and CEO duality, while a strong positive association was observed between ROE and CEO duality. The study suggests that large board size should be encouraged and the composition of outside directors as members of the board should be sustained and improved upon to enhance corporate financial performance.

Coleman,(2007) on his study on examining the effect of corporate governance on the performance of firms in Africa by using both market and accounting based performance measures. Unique data from 103 listed firms drawn from Ghana, South Africa, Nigeria and Kenya covering the five year period 1997-2001 was used and analysis done within the dynamic panel data framework. The researcher use regression and descriptive analysis tools to examine the relationship between variables on the study and the results indicate that the direction and the extent of impact of governance is dependent on the performance measure being examined. Findings show that large and independent boards enhance firm value and that combining the positions of CEO and board chair has a negative impact on corporate performance and CEO's tenure in office enhances a firm's profitability whiles board activity intensity affects profitability negatively. The size of audit committees and the frequency of their meetings have positive influence on market based performance measures and that institutional shareholding enhances market valuation of firms. Finally, results point out that both country and sector characteristics influence the impact of governance on corporate performance. For enhancing performance of corporate entities, the researcher employed return on assets (ROA) and Tobin's q as performance measures and the corporate governance variables used in the study includes Board size, Board independence, Board activity intensity (frequency of meeting), CEO duality, CEO tenure, Audit committee and its characteristics (size of audit committee, NEDs on audit committees, Intensity of audit committee activities) and Institutional ownership.

2.2.3 Empirical Studies in Ethiopia

According to NBE recent issued corporate governance guideline corporate governance plays a vital role in maintaining the safety and soundness of financial system in general and banking sector in particular. The benefit of corporate governances gives way to balanced risk taking and enhances business prudence, prosperity and corporate accountability with ultimate objective of realizing long term Shareholders value, customers and other stakeholders interest .There are very few studies that have been undertaken on the effect of corporate governance on performance banking industry in Ethiopia.

Kassa et al.,(2013,) on their study aims at examining the effect of internal and external corporate governance mechanisms on bank performance and their impact on performance of commercial banks in the absence of organized stock exchange by using quantitative method of data analysis which involved descriptive and inferential statistical analysis and multivariate regression analysis. The study assessed the relationship between selected internal corporate governance mechanism measured by Board size and existence of audit committee in the board and external corporate governance mechanisms measured by capital adequacy ratio, loan to deposit ratio, capital ratio and loan loss provision(CAR,LDRCR and LLP respectively , and bank performance as measured by ROE and ROA. The study used structured review of documents, and commercial banks financial data covering a period 2005 to 2011. The findings indicated that board size and existence of audit committee in the board had statistically significant negative effect on bank performance; whereas bank size had statistically significant positive effect on bank performance. Similarly, capital adequacy ratio, as a measure of external corporate governance mechanism, had statistically significant positive effect on bank performance. In addition the study address that in the absence of organized stock exchange; high government intervention; lack of corporate governance awareness, absence of national standards of corporate governance, as well as accounting and auditing; and weak legal framework to protect minority shareholder rights are the major factors with adverse impact on corporate governance and bank performance in Ethiopia. The study used panel data econometric analysis based on financial and non-financial data collected from all commercial banks in operation from the year 2005 to 2011. Data for this study was obtained from two sources. Audited annual financial statements of the banks covering the period 2005 to 2011 were obtained from the National Bank of Ethiopia (NBE) and data on board characteristics is obtained from each bank in the study.

Ferede, (2012) had used descriptive, correlation and multiple panel linear regression data analysis method to analyze the of impact of corporate governance mechanisms on firms' financial performance using five years data from the year 2007 to 2011 with a sample of eight Ethiopian commercial banks. The researcher employed three financial performance indicators such as return on asset, return on equity and net interest margin, Corporate governance mechanisms include board size, board gender diversity, board members educational qualification, board members business management and industry specific experience, and audit committee size and also three bank specific control variables are included in the study consist of Bank size, leverage and growth. The regression results show that large size board and audit committee negatively influences financial performance; whereas board members educational qualification positively associated with financial performance. While industry specific experience of director positively related with return on asset but it has a negative effect on net interest margin ,the percentage of female directors and board members business management experience does not have a significant effect. The researcher uses both primary and secondary source of data. The secondary source of data is the audited financial statements of the sample commercial banks over a specified period in the study (2007-2011). These data was obtained from National Bank of Ethiopia. The primary data was collected through the use of questionnaires questionnaire to collect data on corporate governance mechanisms variables. Results indicate that the direction and the extent of impact of some corporate governance mechanisms are dependent on the performance measure being examined. All corporate governance variables do not influence the three financial performance indicators in the same direction and their degrees of association may also differ. This is because financial performances indicators are not equally indicate the performance of banks, because financial performance indicators used different formulas with their limitations to indicate the banks performance.

On the topic of the effect of different corporate governance mechanisms on the performance commercial banks of Ethiopia the result of the study shows that proportion of nonexecutive from board characteristics variable, CAR and reserve requirement from regulation proxies had negative and significant impact on the performance of Ethiopian commercial banks. On the other hand concentrated ownership, deposit ratio and availability of audit committee had a positive and significant impact on banks performance. However, the impact of the remaining variables like board size, board ownership, and liquidity on bank performance is negligible. The researcher focus on corporate governance mechanisms Particularly board structure, different regulations, ownership structure and depositors influence, on the performance of the banks and researcher employed ROA and ROE as measure of bank performance Getahun ,(2013).

2.3. Research Gaps

Corporate Governance is important for all organizations regardless of their industry type ,firm size or level of growth. Good Corporate aims at increasing profitability and efficiency of organizations and their enhanced ability to create wealth for shareholders, increased employment opportunities with better terms for workers and benefits to stakeholders. The studies cited in the literature mostly concentrate on the developed countries whose strategic approach and Corporate Governance systems are not similar to that of Ethiopia. In Ethiopia, study done on banks corporate governances are very few in numbers as cited in the literature above .Ferede (2012),Kassaet al,(2013) and Gtahun,(2013) Studied to investigate the corporate governance mechanism and their impact on performance of commercial banks in Ethiopia,

Generally, earlier studies have been made huge contributions to the corporate governance and financial performance; they were attention towards the developed countries. However, developing countries received little attention in various literatures on

issue, consequently, a design feature that works well in one country/industry may not work in another. policy and strategy of any country or industry depends on a number of factors that are unique and contextual to that country or industry . Given the policy objective, the strategy, programs depend on the institutional arrangements of formulating and implementing macro and micro economic structure of the economy as well as the intensity of involving on international economic and financial activities. The policy and administrative strategy designed for each country or industry has to be determined carefully in light of the conditions, objectives and nature of that country or industry. In Ethiopia, few studies have been conducted on corporate governance mechanism and banks financial performance, as the same time majority of these studies were recommending the regulatory body to have better corporate government protection and directive. Based on this the NBE issued the bank corporate governance directive Number SBB/62/2015 which is enter in to force recently as of 21st of September,2015 therefore this study is under taken to investigate the effect of corporate governance on commercial banks financial performance in general and it effect after the implementation of the directives .

CHAPTER THREE

RESEARCH DESIGN AND METHODOLOGY

This chapter deals with the research design and methodology. The caper is organized in to six main parts which are going to explain the research design, sample and sampling technique, sources and tools/instrument of data collection, methods of data analysis, describes Variable Description and Model Specification and finally Specifications of empirical research model is presented.

3.1. Research Design

The methodology to carry out the research is based on the objectives of the paper and the availability of relevant information. To conform to the objective of this research, the primary aim of this study is to examine the effect of corporate governance on commercial banks financial performance. To achieve this objective the study employed an explanatory research design with a mixed approach, more of quantitative will employ. The explanatory type of research design helps to identify and evaluate the causal relationships between the different variables under consideration. Mixed methods research provides better (stronger) inferences. Therefore, by using a mixed approach it is able to capitalize the strength of quantitative and qualitative approach and remove any biases that exist in any single research method (Creswell, 2003).

3.2. Sample and Sampling Technique

The population of the study is all commercial banks operating in Ethiopia. To select sample commercial banks purposive sampling technique is employed. In the sample commercial banks that have complete financial statement for the study period would be included purposively that is based on the age and availability of data for the study period. According to the information obtained from National Bank of Ethiopia there are only 9 commercial banks that have complete financial statements for the study period out of the total commercial banks operating in Ethiopia i.e. 18 banks including the recently merged or swallowed Construction and Business Bank. Those nine commercial banks are selected as a sample i.e CBE,AIB,DB,WB.UB,NIB,CBO,BOA.

3.3 Source of Data and Collection Methods

Regarding sources of data, the study uses both primary and secondary data source. The secondary source of data is the audited financial statements of the sample commercial banks over a period of ten years (2005-2014). These data is obtained from National Bank of Ethiopia. The primary data was collected through the use of questionnaires. Data on corporate governance variables and the changes on bank performance as a result of the implementation of newly issued corporate governance directive is collected by distributing questionnaire to the board secretary and senior management of the sample commercial banks' since they are in a better position to have all the information regarding corporate governance in their organizations. The qualitative data about corporate governance characteristics are also collected by using questionnaire to support the quantitative data which is in addition to the quantitative result obtained by the statistical tools this study also wants to add respondents' responses on the relationship between the variables in the study.

3.4. Procedure of Data Collection

The data were collected from both primary and secondary sources. For collecting the secondary data from the National Bank of Ethiopia and the sample commercial banks the researcher uses the support letter received from the university and the researcher distribute questioners to the selected sample commercial banks board secretary and senior management since they are in a better position to have all the information regarding corporate governance in their organizations and this questioners are derived from previous related studies.

3.5. Methods of Data Analysis

The collected data have been analyzed by using descriptive statistics and inferential statistics analysis methods by using the software called Eviwes 7 version.

In this study to analyze the collected data both descriptive and inferential statistics (fixed effect regression) model data analysis methods are employed. The descriptive statistics is used to quantitatively describe the important features of the variables using mean, maximum, minimum and standard deviations which are used to analyze the variations in explanatory variables. The regression analysis is also used to test the hypothesis and to explain the relationship between corporate governance variables and financial performance measure. Qualitative analysis will used for qualitative data collected through questionnaire.

3.6. Operational Definition Term

In this study, the variables are selected based on alternative theories and previous empirical studies related to corporate governance and firm performance. In accordance with the theory and empirical studies, the independent and dependent variables of the study are identified in order to investigate the effect of corporate governance on firms' financial performance.

3.6.1Dependent Variables

In this study, the dependent variable is variable that is used to measure the financial performance of commercial banks. The frequently used profitability measure was used Return on assets (ROA) is an indicator of how profitable a company is relative to its total assets. ROA gives an idea as to how efficient management is at using its assets to generate earnings and it is calculated by dividing a company's net income by its total assets.

Net income /total asset

3.6.2 Independent Variables

In this study, the independent variables are variables that are used as a determinant of corporate governance of the commercial banks. The independent variables of the study includes board size, board gender diversity, board members educational qualification, board members industry specific experience, size of audit committee and frequency of board meeting

The definitions of the variables are as follows:

- Board size: It can be defined as the number of directors sitting on the board.
- Board gender diversity: Board gender diversity is measured as the number of female directors.
- Board members educational qualifications: It is measured by the proportion of board members who had college degree or higher to the total number of board members. Educational qualification is an important determinant of board effectiveness.

- Board members industry specific experiences: It is measured as the number of directors who served in other financial sectors earlier in the same capacity. It is important for banks to have skilled and experienced directors on board particularly prior experience in the same sector and position.
- Audit committee size: simply it is the number of audit committee. Size of audit committee affects banks' performance. It is likely that small size audit committees effectively communicate in the financial reporting process and problems to be resolved easily.
- Frequency of board meeting: Meeting frequency refers to how many time Board meets on in given period of time one year.

3.6.3Control Variable

In this study two control variables, namely, bank size (BKSZ) and firm age(FAG) included to account its potential influence on banks' financial performance in order to know the selected explanatory variables effect on bank' financial performance.

BKSZ is bank size measured as a logarithm of the year-end total assets

FAG is bank age measure as logarithm of the years since establishment

3.7. Variable Description and Model Specification

In this study, the variables and their relationship were selected based on alternative theories and previous empirical studies related to corporate governance and firm performance. In accordance with the theory and empirical studies, the independent, dependent and control variables of the study were identified in order to investigate the impact of corporate governance variables on firms' financial performance.

3.7.1 Dependent Variable

As already shown in the first chapter, in the context of the problems highlighted the broad objective of this research is to identify banks corporate governance and its effect on bank performance in Ethiopia. In line with the broad purpose statement six hypotheses were formulated for investigation purpose. Hence, the following subsection presents the dependent variable as substitute for banks' performance. Mostly financial performance measures either with accounting-based return, market based return or both. Even though market-based returns are widely acceptable for performance measure by most researchers, they are excluded from this study. This is because of the unavailability of market base data. For example, to use Tobin's Q we need current market price of stock. Such data is not available in Ethiopia as the country has no stock market. In absence of market based data most researches used ROA and ROE as a substitute to performance. In this study the researcher chooses ROA over ROE as substitute to bank performance because of the following reasons. Because ROE weighs net income only against owners' equity, it doesn't say much about how well a company uses its financing from borrowing and bonds. Such company may deliver an impressive ROE without actually being more effective at using the shareholders' equity to grow the company. ROA, because its denominator includes both debt and equity, it indicates how profitable a firm is relative to its total asset and how well management is employing the firms total asset to make profit. Therefore, this study attempts to measure bank performance by using ROA similar to most of the aforementioned researchers.

$$ROA = \frac{\text{NET INCOME}}{\text{TOTAL ASSET}}$$

3.7.2 Independent Variable

In this study, the researcher chooses six independent variables and namely board size , audit committee size , frequency of board meeting , board member gender diversity , board members educational qualifications and board members industry specific experience will be used because these six variable are the major corporate governance variable which affect the performance of commercial banks in Ethiopia .

Board size

It can be defined as the number of directors sitting on the board. According to agency theory limiting board size to a particular level is generally believed to be improving financial performance. The reason is that the benefit of larger boards is outweighed by the poor communication and decision making when the board size is too large. Previous studies found negative effect of board size on firm performanceFered,(2012),Mahboubeh(2013), Xavier,Shuta,Oduor and Mbabaziz,(2012),Fanta,Sirmolo and Kassa (2013),Mahan and Marimuthu(2015) The cost of coordination and processing problems is also high in large boards and this makes decision-taking difficult. On the other hand, smaller boards reduce the possibility of free-riding and therefore have the tendency of enhancing firm performance. For best control and lead of a company there should be an effective board. Board should be inclusive of executive and non executive directors. Researches show that in a small board communication and coordination is more effective than large sized board and also decision making process needs less time and is more accurate.The researcher measures the size of the board by the number of directors serving on such boards and expects this to have a negative relationship with firm performance and test the following hypothesis.

Hypothesis 1

Ha_1: The size of the board is negatively and significantly related to firm performance.

Board gender diversity

Board gender diversity is measured as the percentage of number of female directors divided by the total number of board members. Due to the varying size of boards, a percentage variable provides a more accurate and comparable measurement thus the percentage was taken. Board gender diversity is considered to improve company performance since it provides new insights and perspectives (Bathula, 2008; Erhardt et al., 2003). Female board members will bring diverse viewpoints to the boardroom that is not possible with all male directors.

Hypothesis 2

Ha2: There is a positive and significant attachment between board member gender diversity and commercial banks financial performance.

Board members educational qualifications;- It is measured by the proportion of board members who had college degree or higher to the total number of board members. Educational qualification is an important determinant of board effectiveness. The human capital provided by its board of directors is vital given the corporate board is one of the mechanisms for overseeing the firm and it can arguably provide the knowledge needed to function in the new environment. Personal profile factors of directors such as education and experience is important for board efficiency.

The monitoring role expected to be effectively implemented if the board members are qualified and experienced. Competent board members expected to reduce agency problem. Board of directors is vested with the responsibility of ensuring that the shareholders' money is not wasted, shareholders have a serious interest in ensuring that the board is staffed with well educated and experienced directors (Gantenbein and Volonte, 2011).

Hypothesis 3

- Ha3: There is a positive and significant association between board members educational qualifications and commercial banks financial performance.

Board members industry specific experiences

It is measured as the number of directors who served in other banks earlier in the same capacity as board members. It is important for banks to have skilled and experienced directors on board particularly prior experience in the same sector and position. The effectiveness of board members monitoring role depends on their expertise to fully understand a firm's business situation (Kroll et al., 2008). Thus, industry specific experience of board members expected to improve bank's performance by helping boards effectively reducing agency problem. Appointing directors with related and relevant skills and knowledge to perform task specific duties such as the firm's internal control and procedures will enhance the quality of information gathered and the solution to problems and of the views held and judgments made during the decision-making process (DeZoort, 1998 as cited by Saat, et al, 2011). Directors' specialist knowledge will be valuable to the creation of a strong and informed board (Saat et al., 2011). He claimed that experience of directors enables them to guide, steer and monitor the firm more effectively. In other words, their knowledge of the industry, its opportunities and threats and their connections to the industry participants based on their experience enables them to contribute substantively in the firm performance.

Hypothesis 4

- Ha4: There is positive and significant association between board members industry specific experience and commercial banks financial performance.

Audit committee size;-Audit committees are sub-committee of the board of the company. It is a very important corporate governance mechanism with the objective of enhancing the credibility and integrity of financial information produced by the company and to increase public confidence in the financial statements. Audit committees thus, represent another internal governance mechanism whose impact is to improve the quality of financial management of a company and hence its performance. The establishment of audit committee would lead to better corporate performance. According to the study by Bahreni and Zain, (2013), it showed that when audit committee size is larger, effectiveness of the audit committee is more and it helps the members of audit committee to solve and discuss issues more effectively. Arguments supported by other researchers showed that problems in communication, solving of issues, coordination and decision making will increase when audit committee size is larger. Aldamen et al. (2011) reveals that smaller audit committees with more experience and better educational qualifications are more likely to be associated with positive firm performance. In Ethiopia banking industry, Ferede (2012) found that large number of audit committee has a negative and significant effect on financial performance. He added that Limiting audit committee size to reasonable number improves audit committee effectiveness.

Here in this study, the researcher want to investigate the effectiveness of audit committee size on the performance of banks .Based on these, we expect that there is a negative and significance relationship between audit committee size and banks performance.

Hypothesis 5

Ha5:- There is a negative and significant relationship between audit committee size and financial performance

Frequency of board meeting:-Meeting frequency refers to how many time Board members meet within a year. Measuring the intensity and effectiveness of corporate monitoring and discharging is the frequency of board meetings (Jensen M. , 1993). Meeting Frequency has a significant negative impact on ROA and an increasing in meeting frequency will reduce the ROA (Ms.S.Danoshana and Ms.T.Ravivathani, 2013). Moreover, Akpan (2015) found that board meetings negatively and significantly relate with company performance. Another study conducted on public listed companies in Malaysia using five years data 2003 to 2007 of 328 companies, shows that the higher the number of meetings the worse the firm performance (Amran, 2011). Whereas, Karamanou et al (2005) found a positive association between frequency board meeting and management earnings forecasts, using a sample of 157 firms in Zimbabwe from 2001-2003; Mangena and Tauringana (2008) report a positive relationship between board meeting frequency and corporate performance.=

Similarly in a study of the sample of 169 listed corporations from 2002-2007 in South African, a statistical significant and positive association between the frequency of board meeting and corporate performance exist (Ntim and Osei, June 2011). This implies that the board of directors in South Africa that meet more frequently tend to generate higher financial performance. Moreover, Ntim and Osei (2011) found a statistically significant and positive association between the frequency of corporate board meetings and corporate performance, implying that South Africa boards that meet more frequently tend to generate higher financial performance.

Hypothesis 6

Ha_6: The number of board meetings is negatively and significantly related to firm performance.

3.7.3 Control Variable

In this study two control variables, namely, bank size (BKSZ) and firm age(FAG) included to account its potential influence on banks' financial performance in order to know the selected explanatory variables effect on bank' financial performance.

BKSZ is bank size measured as a logarithm of the year-end total assets

FAG is bank age measure as logarithm of the years since establishment

3.7.4 Specifications of Empirical Research Model

To estimate the Effect of corporate governance on the financial performance of sample commercial banks in Ethiopia the following general empirical research model is developed.

$$\mathbf{Y}_{it} = \boldsymbol{\beta}_0 + \boldsymbol{\Sigma\beta}_K \mathbf{X}_{it} + \boldsymbol{\varepsilon}_{it}$$

Where:

- ✓ Y_{it} represents the dependent variables ROA of bank *i* for timeperiod *t.*
- ✓ β_0 is the intercept
- ✓ β_K represents the coefficients of the X_{it} variables
- ✓ X_{it} represents the explanatory variables (BS , FD, BEDQ, INSE, AUS, FBM) of bank *i* for time period *t.*
- ✓ ε_{it} represents The error term

The above general empirical research model is changed into the study variables to find out the impact of corporate governance mechanisms on firms financial performance as follows:

$$ROA_{it} = \beta_0 + \beta_1(BS_{it}) + \beta_2(FD_{it}) + \beta_3(BEQ_{it}) + \beta_4(INSE_{it}) + \beta_5(AUS_{it}) + \beta_5(FBM)_{it} + BKSZit + FAGEit + \varepsilon_{it}$$

Where:

i denote banks ranging from 1 to 9

t denote years ranging from 2005 to 2014

Dependent Variables

ROA *it* Return on Asset for *i*th bank and time period *t*

Independent variables

BS *it:*-Board Size for *i*th bank and time period *t*

FD*it* :-Female Directors on the board for *i*th bank and time period *t.*

BEQ*it* *;*-Board members Educational Qualification for *i*th bank and time period *t.*

INSE*it ;*-Board member's industry specific experience for *i*th bank and time period *t.*

AUS*it ;*-Audit committee size for *i*th bank and time period *t.*

FBM*it:*-frequency of board meeting for ith bank and time period t.

Contro variables

BNKZit:- Bank size

FAGEit:- firm age

CHAPTER FOUR

RESULTS AND DISCUSSION

This chapter presents the descriptive statistics, correlation analysis and regression analysis of the study variables. 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 output of the regression fixed effect model.

4.1. Descriptive Statistics of Variables

This section discussed the summery statistics of each variables of the study. The variables include the dependent, independent and control variables. The dependent variable used to study the financial performance of commercial banks is Return on Asset (ROA). The explanatory variables were board size, board gender composition, board competency, board experience in the Finance sector, meeting frequency of board and size of audit committee. Whereas the control variable used in this study was firm size measured by natural logarithm of total asset of the commercial banks and firm age measure by the logarithm of as the number of years since the company is incorporated.

Table 4.1. Descriptive statistics result summary

	ROA	BS	AUS	BEDQ	FBM	FD	INSE	BKSZ	FAG
Mean	0.026503	9.955556	1.311111	7.944444	10.22222	1.022222	1.866667	22.53574	1.133443
Median	0.029067	10.00000	2.000000	8.000000	12.00000	1.000000	2.000000	22.51595	1.146128
Maximum	0.046681	12.00000	3.000000	11.00000	12.00000	2.000000	4.000000	26.21560	1.707570
Minimum	-0.018705	8.000000	0.000000	5.000000	4.000000	0.000000	0.000000	18.67530	0.000000
Std. Dev.	0.009998	1.150585	1.056222	1.440670	3.344550	0.792915	0.950458	1.300477	0.319701
Observations	90	90	90	90	90	90	90	90	90

Source: Eview 7 result based on the data obtained from sample commercial banks

The mean values tell about the average size of board, size of audit committee , board competency ,female board, board experience in the finance sector, board meeting frequency , average size of banking industry and ROA . Standard deviation has been used to analyze the variations in explanatory variables, control variables as well as in ROA.

The average value of return on asset, which measures financial performances of Ethiopian commercial banks in this study, for the sample Ethiopian commercial banks is 0.027(0.0265) with a maximum and minimum value of 0.047(0.04668) and -0.019(0.0187), respectively as presented in the table 4.1 above. The standard deviation is 0.0099(0.009998) from the average value 0.027. The standard deviation of 0.0099 suggests that there is no wide dispersion in the return on asset of the sample commercial banks.

In the explanatory, the average size of board for Ethiopian commercial banks is 10 members (mean=9.9) with a minimum board members of 8 and maximum board member of 12.The standard deviation indicates10. The standard deviation of 1.15 suggests that there is no wide dispersion in the board size of the sample Ethiopian commercial banks.

Regarding to audit committee size, the sample Ethiopian commercial banks have a mean value of 1.311 with a minimum of zero audit committee and a maximum of 3 audit committee members. The standard deviation is 1.056 from the mean. This indicates that there are commercial banks which don't have audit committee .The standard deviation of 1.05 suggests that there is no wide dispersion in the audit committee size of the sample Ethiopian commercial banks.

As we have seen from the above table 4.1, the competency of Ethiopian commercial banks board members, as measured by holding college degree or above, has a mean value of 8(7.94) with a minimum of 5 members and maximum of 11 members. This shows that board members are competent and educated. The standard deviation is 1.44 from the mean value of 8. The standard deviation of 1.44 suggests that there is no wide dispersion in the board competency of the sample Ethiopian commercial banks.

Concerning gender composition, on average 1 board of director (mean= 1.02) of commercial banks are females with a minimum of null female director and maximum of 2 female directors. It suggests that the composition of gender of sample Ethiopian CB's boards, as measured by proportion of director position held by women, is low since its mean value is only 1.02 during the last ten years. The standard deviation indicates that for the sample Ethiopian CB's female directors vary by 0.79 from the average value of 1.02.

The other explanatory variable is board of directors’ experience in the finance sector. The board of sample CB's has a mean of 1.86 with a minimum of null and maximum of 4 as measured by the proportion of directors who had experience in the finance sector. This shows that Ethiopian commercial banks board of directors’ experience in the finance sector is low for the last ten years. The standard deviation is 0.95 from the mean value of 1.86.

When we come to the meeting frequency of the sample Ethiopian commercial banks ,board of directors conduct meeting minimum of 4 times and maximum of 12 times and on average 10 times in year. The standard deviation is 3.34 from the mean of 10.22.

When we see the control variable, the mean value of CB's size as measured by the natural logarithm of total asset is 22.54 (22.5354) with having a maximum value of 26.22(26.215) and minimum values of 18.67. The standard deviation of commercial banks size is 1.3. The standard deviation of 1.3 suggests that there is no wide dispersion in the size of the sample Ethiopian commercial banks.

The other control variable is firm age, mean value of CB'S age measure by the log of the firms age since the establishment is 1.133 with having a maximum value of 1.7075 and minimum values null. The standard deviation of commercial banks age is 0.319. The standard deviation of 0.32 suggests that there is no wide dispersion in the age of the sample Ethiopian commercial banks.

4.2. Regression Results and Discussion

This section of the study presents the results and discussions of the regression results. In order to examine the effect of corporate governance elements on sample Ethiopian commercial banks financial performance panel linear regression model was estimated. The regression analysis enables the researcher to empirically test the proposed hypothesis and to achieve the research objective. The method of least squares has some very attractive statistical properties that have made it one of the most powerful and popular methods of regression analysis (Gujarati, 2003). Thus, by conducting the appropriate diagnosis tests fixed-effect Model estimation was used in the model.

4.2.1. Diagnostic Tests of the Data

The data sets were tested for the classical linear regression model assumptions before running the model. Brooks (2008) suggests five critical assumptions that must be met before utilizing OLS estimation in order to validly test the hypothesis and estimate the coefficient. The classical linear regression model assumptions and their diagnostic tests are discussed below.

1. The average value of the errors is zero. If a constant term is included in the regression equation, this assumption will never be violated. So that in the model of this study a constant term is included. As a result this assumption is not violated.

2. The assumption of homoskedasticity. This assumption requires that the variance of the errors to be constant. To check this assumption White test is conducted for the model. (See table 4.2). In the model there is no problem of heteroscedasticity or the error variance is constant since the p-value is not significant, meaning that p-value is 0.20 which is greater than 0.05. This means the null hypothesis was not rejected which says that the error variance is constant.

Table 4.2.Heteroscedasticity test

H0: The variance of the error is Homoscedastic

H1: The variance of the error is Heteroscedastic

Heteroskedasticity Test: White

F-statistic	1.284878	Prob. F(43,46)	0.2020
Obs*R-squared	49.11101	Prob. Chi-Square(43)	0.2416
Scaled explained SS	44.64349	Prob. Chi-Square(43)	0.4025

Eviews 7 test result based on the data obtained

3. No autocorrelation between the disturbances. It is assumed that the errors are not correlated with one another. If the errors are correlated with one another, it would be stated that they are ‘serially correlated’. A test of this assumption is therefore conducted. The first test was Durbin-Watson which is shown in the regression output of the mode.. Durbin-Watson is a test for first orders autocorrelation. It tests only for a relationship between an error and its immediate previous value. Therefore, in addition to DW test it is desirable to conduct

Breusch-Godfrey Serial Correlation LM test to examine a joint test for autocorrelation that will allow examination of the relationship between error term and several of its lagged values at the same time. Thus, Breusch-Godfrey test is also conducted for the model (see below table 4.4) and found problem of autocorrelation for the model, meaning that p-value of the test resulted 0.00 which is less than 0.05.

Table 4.3. Autocorrelation test

H0: The errors are uncorrelated with one another

H1: The errors are correlated with one another

Breusch-Godfrey Serial Correlation LM Test:

F-statistic	11.45295	Prob. F(2,79)	0.0000
Obs*R-squared	20.22975	Prob. Chi-Square(2)	0.0000

Eviews 7 test result based on the data obtained

4. Model misspecification error: With regard to model misspecification error Ramsey reset test is conducted for the model. (See table 4.5). The Ramsey regression specification error test result for the model is significant, (i.e. test statistics probability is 0.00). The researcher fear to rejects the null hypothesis. Thus, the result indicates there is model specification error in the model of the study.

Table 4.4.Model specification error (linearity) test

H0: The model functional form is appropriate

H1: The model functional form is inappropriate

Ramsey RESET Test

	Value	df	Probability
t-statistic	2.607928	80	0.0109
F-statistic	6.801289	(1, 80)	0.0109
Likelihood ratio	7.343535	1	0.0067

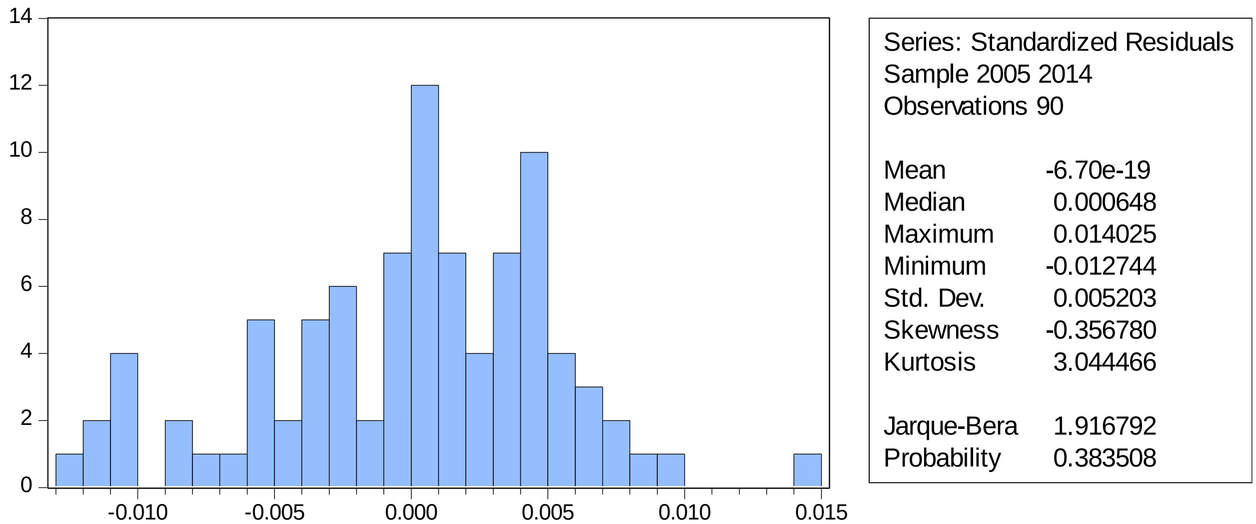
Eviews 7 result based on the data obtained

5. Normality assumption (The disturbances are normally distributed): Bera-Jarqu normality test which is the most commonly used normality test was conducted for the model after estimating the regression (Figure 4.1.). The p-value is 0.38 which is insignificant for the model and the researcher failed to reject the null hypothesis, which says the residual value is normally distributed. Moreover, kurtosis is 3.04 which is near to 3. Therefore, there is no normality problem on the data used for this study.

FIGURE 4.1.Normality test

H0: Residuals are normally distributed

H1: Residuals are not normally distributed



Source: Eviews 7 result based on the data obtained.

Fixed effect Versus Random effect

It is also necessary to determine whether the fixed effect or random effect approach is appropriate. A common practice in corporate governance research is to make the choice between both approaches by running a Hausman or redundant fixed effect model tests. Therefore; a redundant fixed effects test was conducted to determine whether it is appropriate for the model.

Table 4.5. Redundant Fixed Effects Tests

Test period fixed effects

Effects Test	Statistic	d.f.	Prob.
Period F	1.463988	(9,72)	0.1780
Period Chi-square	15.124712	9	0.0876

Eviews 7 result based on the data obtained

In the model the p-value is insignificant in the case of time-fixed effects where only the period fixed effects are allowed. As a result the time-fixed effect approach was used. Hence, with time-fixed effects, the intercept is allowed to vary over time but assumed to be the same across banks at each given point in time. From the above tests of basic linear regression model assumptions for OLS estimation three of them are fulfilled, the results obtained from the regression model in this study are consistent, free from bias and efficient since the assumption holds and the next step is analyzing and discussing the outputs of the regressions.

Table 4.6. Fixed effect result

Dependent Variable: ROA

Method: Panel Least Squares

Date: 06/11/16 Time: 16:03

Sample: 2005 2014

Periods included: 10

Cross-sections included: 9

Total panel (balanced) observations: 90

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	0.012084	0.023917	0.505241	0.6149
BS	-0.003841	0.001216	-3.158828	0.0023
AUS	-0.002501	0.000791	-3.160769	0.0023
BEDQ	0.001877	0.000782	2.401163	0.0189
FBM	0.002590	0.000361	7.177250	0.0000
FD	2.60E-05	0.001241	0.020955	0.9833
INSE	0.003200	0.001058	3.025460	0.0034
BKSZ	-0.001203	0.001144	-1.051846	0.2964
FAG	0.031462	0.004921	6.394084	0.0000
	Effects Specification			
Period fixed (dummy variables)				
R-squared	0.729116	Mean dependent var		0.026503
Adjusted R-squared	0.665158	S.D. dependent var		0.009998
S.E. of regression	0.005785	Akaike info criterion		-7.290188
Sum squared resid	0.002410	Schwarz criterion		-6.790226
Log likelihood	346.0585	Hannan-Quinn criter.		-7.088574
F-statistic	11.39981	Durbin-Watson stat		1.220580
Prob(F-statistic)	0.000000			

Source: Eviews 7result based on the data obtained

As it is summarized in the table 4.6.above, the R2 for the model is 72.9 percent the adjusted R2 is 66.5, Which means that 72.9 percent of the variation in return on asset was explained by the independent and control variables used in this study in other words the explanatory variable describes the dependent variable 72.9percent, 27.1 percent of variation in return on asset is due to other many factors that are not included in this study. The R2 results indicate the overall goodness-of-fit of the model used in this study. The adjusted R2 value is 66.5 percent, which indicates that 66.5 percent, of the variation in the Ethiopian commercial banks return on asset, was explained by the explanatory variables in the model. The adjusted R2 measures how well the model fits the data by taking into account the loss of degrees of freedom associated with adding extra variables. Therefore, the model fits the data. In addition; the F-statistic shows the overall significance of variables in other words the significance of the model slope parameters jointly. The F-statistics of the model is 11.39 and the null hypotheses of the model were rejected. Therefore, the model variables are jointly significant. The model adequately describes the data. Here one can infer from the results of R-squared and F-statistics that the implemented model of this research are well fitted that corporate governance mechanisms have a significant effect on banks' financial performance.

4.3.2. Corporate Governance: Results and Discussion

Board size

As we observed from the above table 4.6, this study found a negative and statistically significant association between boards size (BS) with coefficient of -0.003841and (p-value of 0.0023< 0.05) with return on asset. It implies that the numbers of board of directors' are negatively related with commercial banks' financial performance. In other words, the higher the number of board members of commercial banks, the lower their financial performance achievement is and vice versa. The result indicates that small boards are more effective in monitoring and controlling banks management and it help to reduce costs.

The finding supports the argument that an increase in board size would leads to less effective and efficiency and monitoring of the activities of management. The result is consistent with prior studies which argue that too larger boards have their own cost and an increase in board size leads to less effective monitoring due to coordination and process problems inherent in large board size and communication and decision-making problems increasingly affects company performance when the number of directors increases.(Nazar and Rahim(2015);Kassa et al,(2013) ;Ferede, (2012);Jense,(1993);Almanaseer et al.(2012); Nazar, Rahim(2015) ;Amran (2011) ;Ayorinde et al (2012); Mahboubeh,(2013)) Therefore, the result shows that board size has negative and significant influence on company performance.

Subjective question was also asked whether the respondents believe the number of board size affect banking industry financial performance **(Question No.7 Appendix I).** Almost all (95%) of the respondents said "NO" and they justify that too large and too small board is not appropriate to run the responsibility of the board .Banks need to have reasonable number of directors in order to perform their task effectively and efficiently. Good justification giver for this question was that boards with too large members lead to problems of coordination in decision making. Small board size was better to promote critical, genuine and intellectual deliberation and involvement among members which presumably might led to effective corporate decision making, monitoring and improved performance depend on the factors such as experience and education of the directors. National bank of Ethiopia set the minimum number of director to be 9.The outcome of the analysis of both quantitative and qualitative data indicates that there is a negative relationship between board size and financial performance of sample commercial banks in Ethiopia. Therefore, both the regression and qualitative result support the hypothesis.

Board Gender Composition

The relationship between board gender composition (FD) and the measure of financial performance has (p-value of 0.9833> 0.05). This is insignificant and alternative hypothesis predicts that the number of women directors on the board is positively associated with financial performance. The insignificant coefficient of the percentage of women directors does not support this hypothesis. Therefore, this study does not support the view that gender diversity leads to higher banks financial performance. Some previous studies document a positive and insignificant effect of the role of women on boards and find that women enhance the quality of decision making and firm performance (Ferede, (2012) ;Bathula,(2008)).all found insignificant relationship between board gender composition and firm performance. However, this study does not find a significant positive association between percentage of women directors and banks financial performance. This may be due to the relatively small proportion of board members who are women as shown in the descriptive analysis section, which does not permit them to be powerful enough to make a difference to monitoring. This result does not necessarily contradict the notion that women's presence on boards may be useful and positive in general. Nevertheless, the low number of women on the boards of sample Ethiopian commercial banks does not give them sufficient monitoring power.

In the qualitative question (**Question No.8 Appendix I**) majority (80%) of respondents said 'yes' and justified as board gender diversity is important since almost half of the country's population is female, they can represent major potential customers and help banks to have links with this potential customers and in addition some the respondents says that females are critical thinker and it is easy for them to take care of customers than men. But, simply the presence of female directors will not improve banks operation and performance unless they are qualified and competent. Whether gender diversity help improve banks operation and performance it depends on factors such as experience, education and assertiveness of female directors.

Board Members Educational Qualification

Board members educational qualification (BEDQ) has a positive effect on measure of commercial banks financial performance. Board member’s educational qualification explains the variations of the financial performance of commercial banks with a coefficient of 0.001877, and is statistically significant at p-value of 0.0187which is less than 5%percent. The result indicate that the increase in the proportions of directors who had college degree and above have a significant positive influence on the financial performance of commercial banks and vice versa. In other words the higher the number of directors who had college degree and above sitting on the board the higher the financial performance of sample commercial banks in Ethiopia and vice versa. This suggests that the presence of qualified directors on the board plays an important role in carrying out the boards monitoring responsibility and in improving financial performance. the alternative hypothesis for board educational qualification predicts that there is a significant positive relation between board members educational qualification and banks financial performance. Thus, the result is in line with the proposed alternate hypothesis. Thus, there is a significant positive relationship between board members educational qualification and financial performance of commercial banks in Ethiopia. This result supports the finding discovered by Amran ,(2011) ; Ferede (2012). They argues that directors with higher education are better in managing the business operation and controlling agency problem than less educated this reduce agency cost. Educational qualification affects the oversight and monitoring role of boards of directors. The result support the view that educational qualification is potentially important since the ability to seek and interpret appropriate information is essential for the efficient operation of banks and the effective control or guidance of management by boards of directors. The qualification of directors as measured by the number of directors who had college degree or above has significantly influences bank performance.

Respondents were asked to reflect their view whether they feel or not that educational qualification of directors have affects their monitoring and controlling efficiency and effective efficiency (**Question No.9 Appendix I)**. Almost all of the respondents (95 %) said “yes”. The best justification given is that directors need to have a minimum of college degree in order to read and interpret the financial statements and other reports given by the banks management, give right direction properly, and able to give strategic leadership. Boards of directors make decision after analyzing and carefully understanding the technical documents submitted by management as a report. In addition, they stated that education plays a key role not only in the finance sector but also in any other sector of the economy. Thus, educational qualifications of directors play a great role in board decision making. Both the regression result and the qualitative analysis indicate that educational qualification of directors is important factor to improve financial performance of commercial banks in Ethiopia. Thus, there is a significant positive relation between board competencies (educational qualification and CB’s financial performance).

Industry Specific Experience of Directors

Hypothesis 4 expected that industry specific experience of directors (INSE) is positively associated with banks financial performance. As expected, a positive association is found between industry specific experience and return on asset with a positive coefficient and p -value of 0.0032 and 0.0034 respectively .It means the higher the proportions of directors who had earlier working experience in the finance sector the higher the financial performance (as measured by return on asset) of sample commercial banks in Ethiopia and vice versa.

Respondents were asked a subjective question (**Question No.10 Appendix I**) about directors' prior experience in the financial sector. All (100%)of the respondent says "yes" and they justified that board of directors who had an experience in the financial sector is highly important because they share the experience they had, challenges they faced and actions they took in their previous job. The qualitative result and regression result support the alternative hypothesis of Board experience in the finance sector is positively related with CB’s financial performance.

Audit Committee Size

Audit committee size (AUS) on Commercial banks’ financial performance has negative and significant impact with a coefficient of -0.002501 and p- value of 0.0023< 0.05 for performance measure. Which means that the larger the audit committee is the lower will be the financial performance of commercial banks as measured by return on asset. Therefore, the alternative hypothesis that states size of audit committee has negative relationship with banks financial performance is accepted.

The result is consistent studies conducted previously by (Kassa et al(2013); Ferede,(2012); Aldamen et al,(2011); Reveals that smaller number of audit committee with more experience and better educational qualification are more likely to be associated with positive firm performance and they found that the size of the audit committee negatively influences performance. This study result supports the notion that a certain minimum number of audit committee members may be relevant to the quality of financial reporting and to enhance financial performance. Free-riding and difficulty to reach in consensus in large groups inversely affect financial performance. Therefore, the outcome of this variable is in line with the alternate hypothesis.

The respondents were also asked to reflect their views regarding the size of audit committee. For the subjective question **(Question no. 11 appendix I)** majority of the respondents (60 percent) said "no" meaning that increasing the size of audit committee will not improve performance. The respondents justified that it not the size, but having an effective board audit committee will improve the performance of the institutions. They added that size is not an issue in audit committee but their experiences and commitment to review an internal and external audit report. So the alternative hypothesis is supported. Therefore, both the regression and qualitative result support the hypothesis.

Meeting Frequency

Return on Asset with Meeting Frequency (FBM), coefficient and p- value of 0.00259 and 0.000, respectively. This result shows that, Meeting Frequency has a significant positive impact on ROA and an increasing in meeting frequency will improve the financial performance of firms. So meeting frequency has significant positive impact on the firm performance. Result of this study does not support the tested alternative or null hypothesis, which states the meeting frequency and banks performance have negative relationships.

Respondents asked about their view regarding the impact of board meeting frequency on the performance of Ethiopian baking industry **(Question no. 12 appendix I)** that more than half (65%)of the respondents said high meeting frequency generate high performance and said that it depends on the agenda and quality of the meeting not the frequency while the rest said the reverse. The best justification given by respondent was board that at least meet once in month can better follow up the performance, challenges of the institution and monitor their decision implementations. They believe that, by having a good agenda board who meet most frequently will generate higher financial performance. Therefore the result of both regression and qualitative data does not support the outcome expected by this study.

Effect of New Corporate governance Directive

In addition to the above subjective questions respondents were asked to reflect their view regarding the change that they observe as a result of the newly issued directives on their institutions in terms in board structure (Question No.13 and 14 Appendix I). In relation to the change in performance almost all of the respondents said "yes" and they justified that even if it is difficult to quantify the performance since the directive was issued recently**,** since the Corporate governance code covers every aspect of the organizational set up, right from how resources are generated and how they are utilized and it guide the share holders and the stack holders of the corporation. and it has become an important factor in managing organizations in the current global and complex environment and protecting the interests of its stakeholders including shareholders, creditors, regulators and the public it is expected that in the near future the performance of the firms are improved and the improvement of corporate governance practices is widely recognized as one of the essential elements in strengthening the foundation for the long-term economic performance of corporations. In addition in relation to the structure of the board the respondents said "yes" which men as there is change in board structure after the implementation of the newly issued corporate directive.

The main justification given by the respondents were previously the minimum board structure were determined as they like because the national bank of Ethiopia set the maximum number of board structure , But if we see the change in each explanatory variables ; as we show from the descriptive statistics result the minimum number of directors for the last ten years were eight but the currently issued directives forced the Ethiopian commercial banks to have minimum nine (9) member of directors , the board of directors as a group provide a mixture of gender and competencies, board members to meet once in a month to follow up the status of the banks, force the commercial banks to have audit committee comprise of at least three directors having accounting or auditing experience in the field of finance which changes the last ten years audit committee history as we have observed from the descriptive statistics there are commercial banks do not have audit committee for the last ten years. Because, there is a growing consensus that corporate governance has a positive relationship with firm performance.

4.3.3 Control Variable and Discussion

Bank size

Commercial bank's size which was measured by Logarithm of Total asset has a statistically insignificant (p-value of 0. 2964> 0.05) with negative coefficient of -0.001203 relationships with the financial performance of sample commercial banks.

Firm Age

Commercial bank's age which was measured by Logarithm of the years since the establishment has a statistically significant (p-value of 0.000< 0.05) with positive coefficient of 0.031462 relationship with the financial performance of sample commercial banks.

CHAPTER FIVE

SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

5.1. Summary and Conclusions

In the final chapter to this study the major findings of the study is summarized; conclusions are drawn based on the finding, recommendations are forwarded.

Banks are the important component of any financial system. They play important role in the economy by transferring fund from the surplus unit to deficit unit of the economy. The efficiency and competitiveness of banking system defines the strength of any economy. Like other developing countries in Ethiopia banks plays a vital role in the process of economic growth and development. Sound corporate governance encourages the efficient use of resources and provides for accountability for those resources by managers. Institutions that practice good corporate governance are more likely to achieve institutional objectives and goals. Good corporate governance should thus be of prime concern to owners and other stakeholders of the institutions. In fact, good corporate governance helps promote the general welfare of the society and should be of interest to the general public and governments. Corporate Governance broadly refers to the mechanisms, processes and relations by which corporations are controlled and directed. The prime objective of this study was to examine the effect of corporate governance in financial performance of Ethiopian commercial banks by using nine Ethiopian commercial banks with a data covering ten years period from the year 2005 to 2014. Specific objectives were to investigate the effect of corporate government variables on financial performance of the firms. In this study both primary and secondary sources of data were employed to analyze the relationship between the variables in the study. The dependent variables used in this study was return on asset and the independent variables were board size, board composition in terms of gender ,audit committee size, frequency of board meeting, industry specific experience and educational qualification of board members. Also two control variables bank size (BKSZ) and firm age (FAG) were included to account its potential influence on banks' financial performance in order to know the selected explanatory variables effect on bank' financial performance. Based on the results of the analysis tools the researcher made the following conclusions.

From this research, it is found that all the corporate governance elements do not affect the performance of selected commercial banks in the same way. Based on the results of the descriptive statistics and regression analysis, the researcher made the following conclusions. Based on the descriptive statistics the financial performance of sample commercial bank is 2.65 percent, as measured by return on asset.. The sample commercial banks board is characterized by the presence of qualified directors and. But, the board is dominated by male and consists of very minimum numbers of directors who had prior experience in the finance sector and also there are commercial banks which do not have audit committee for the last ten years.

The regression result shows that board size and audit committee size significantly and negatively influence sample commercial banks financial performance. No statistically significant relation was found between presence of female directors and financial performance. However, this is due to very small numbers of female directors as observed in the descriptive statistics which does not permit them to be powerful enough to make a difference to monitoring. Moreover, the qualitative analysis revealed that qualified and competent female directors help improve banks operation and monitoring performance. Therefore, only the presence of qualified and competent female directors helps improve banks performance. Board members educational qualification significantly and positively influences the financial performance of sample commercial banks. The presence of qualified directors on the board plays an important role in carrying out the boards monitoring responsibility and in improving financial performance. Thus, board members educational qualification has a significant positive effect on banks financial performance. While industry specific experience of director positively and significantly influence return on asset and Meeting Frequency has a significant positive impact on performance measure in this study and an increasing in meeting frequency will improve the financial performance of Ethiopian commercial banks. In general, the findings suggest that banks with effective corporate governance mechanisms improve financial performance.

5.2. Recommendation

This study examined the Effect of corporate governance on firms' financial performance by taking evidence from selected commercial banks in Ethiopia. On the basis of the findings and conclusions reached, the following recommendations were forwarded. Attention should be given for the board size of banks to be small in number to optimal level with better educational qualification since small board size with better educational qualification is more effective in monitoring managers and help to improve performance. This study revealed that the boards of banks are dominated by male and board gender diversity is very limited in Ethiopian commercial banks for the last ten years. Thus, there is much to be done to improve the gender balance of boards in Ethiopian banks with a great care about their qualification and competency. This research found that there are limited numbers of experienced board of directors in commercial banks .But the experience of board of directors in the finance sector is positively and significantly affects the performance of firms. Therefore, the researcher recommends that Ethiopian commercial banks should include experienced board in other financial sector to improve their financial performance as if the helps the firms to improve their performance by sharing their past experience. Finally, the researcher recommends that Ethiopian commercial banks should make their audit committee size small to improve their performance. Because, as this study revealed large size audit committee negatively influences performance.

5.3. Limitations

As any other study, this study is subject to some limitations. In this study the sample banks were selected purposively based on the age and availability of data this is because there are only nine commercial banks that have complete data for the study period. Mostly financial performance measures are either with accounting-based return, market based return or both; but on this study it is limited to accounting measure only because of the unavailability of market base data. The other limitation of this of study was that limited to examining the Effect of internal corporate governance on firms' financial performance by taking evidence from commercial banks in Ethiopia for the period of ten years, from 2005 to 2014.

5.4. Implication for Future Study

By taking evidence from other industries and increasing the number of observations through the use of large sample size and long year’s data and including more internal and external corporate governance variables, the relationship between corporate governance variables and firms' financial Performance can also be further explained.

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APPENDICES

ST MARY'S UNIVERSITY

SCHOOL OF GRADUATE STUDIES

MBA PROGRAM

RESEARCH QUESTIONNAIRE

Appendix I

Dear respondents these questionnaire are intended to collect data for research to be conducted on the Effect of corporate governance on financial performance of Ethiopian banking industry. It is only for educational purpose. I kindly seek your kind assistance in completing the questionnaire which would take approximately 15 to 20 minutes of your valuable time. Your responses will be treated as **"strictly confidential" So, please, you are highly requested to answer genuinely as much as possible**..

Note: - Kindly tick (√) you feel appropriate for your feedback for part one .

For any information please do not hesitate to contact me mobileno.0912198234/0913970659 or Email address:-firehiwot.2003@gmail.com

Thank you in advance for your cooperation!!!

Part I: Personal information

1. Educational qualification

Diploma Collegedegree Masterdegree Above

2. Gender: Male Female

3. Do you sit on Board as a member? Yes No

Part two

- Please use numbers only to fill the table below for each period.

No.	Variables	Fiscal years (GC)								
		2006	2007	2008	2009	2010	2011	2012	2012	2014
1	Total number of board of directors									
2	Total Number of females in the board									
3	Total number of audit committee members									
4	Total Number of directors who have degree and above									
5	Total Number of directors who works in the same institution before joining your organization									
6	How many time does the board members conduct meeting in a year									

Part three

- **General Question**

7. Do you believe that board size affects banks performance? **Yes** **No**

How? Please justify it--

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8. Does the presence of female board of directors' in terms of board diversity helps

Improve the banks operation and performances? **Yes** **No**

Why? Please justify it --

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9. Does the educational qualification of directors have any significant effect on their monitoring and controlling and their efficiency? **Yes** **No**

Give your reasons--

--.

10. Are there any board members who had previous working experience on banking business now in your organization? **Yes** **No**

In what ways do these members contribute better than other directors? ----------------------------
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11. Do you believe that increasing the size of audit committee improve their effectiveness? **Yes** **No**

How? Please justify it ---

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12. Do you believe that more frequently meeting can generate higher financial performance**?** **Yes** **No**

Please justify it? ---

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13. Do you believe that the newly issued corporate governance Directive Number SBB/62/2015 which could bring any change to your bank or enhance your profitability? **Yes NO**

please justify it?--.

14. Is your bank board structure changed after the implementation of Corporate governance Directive Number SBB/62/2015 in terms of board size, audit committee size ,gender composition, educational qualification, meeting frequency and experience ? **Yes** **NO**

please justify it?--.

Thank You Once Again!!!

April, 2016

Appendix II

List of Sample commercial banks

1. Commercial bank of Ethiopia
2. Construction and business bank
3. Dashen bank
4. Awash international bank
5. Wegagen Bank
6. Bank of Abyssinia
7. Cooperative bank of oromia
8. Nib international bank
9. United bank