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Relationship between Corporate Governance and Firm Performance

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ABSTRACT

This research focuses on the measurement of the quality of corporate governance and on whether there exists a relationship between corporate governance and firm performance for a sample of the Top 100 companies. With reference to the battery of models available from the literature and the Code of Corporate Governance applicable to Mauritius, a checklist measuring the effect of 13 key factors was developed and studied in relation to the Taffler model. Analysis from the results shows that on the overall, there is no difference in performance for companies having poor and excellent quality of governance. Hence no significant relationship has been found between corporate governance and financial performance.

1.Introduction

Major notorious accounting failures the world over have dented investor confidence and have raised several questions on the effectiveness of a firm's internal control system and governance structures. Indeed, the theme making the headlines for the past years is corporate governance. Broadly speaking, CG is all about making sure that decisions are made effectively. This impetus towards corporate governance has been due to many factors. For instance, it matters for shareholders as it is a shield against abuse of directors while improving access to capital for the company itself and instilling financial stability in the market. The broad aim of the study is to tap the actual compliance with the CG provisions by Mauritian firms, and more importantly to probe into the relationship between CG practice and its effect on performance. In fact the specific objectives set for this research are to i) generate a conceptual framework for CG practices to assist towards the establishment of a CG score ii) Analyze and gauge the state of CG practices of Mauritian companies and iii) to examine the possible

relationship between CG practices and firm performance based on a sample of the Top 100 companies in Mauritius. The rest of this paper is organised as follows: section 2 reviews the previous literature and gives a brief overview of the CG situation in Mauritius, section 3 discusses the research methodology, section 4 provides the analysis of results and section 5 concludes the paper.

2.Literature Review

2.1 Understanding Corporate Governance

Corporate governance is sometimes viewed as a business culture fostering economic growth by building up confidence of investors (The HIH Royal Commission Report 2003). Others (Schmidt and Tyrell, 1997) adopted a more concise definition relating to a company: "corporate governance is the totality of the institutional and organizational mechanisms, and the corresponding decision-making, intervention and control rights, which serve to resolve conflicts of interest between the various groups which have a stake in a firm and which, either in isolation or in their interaction, determine how

important decisions are taken in a firm, and ultimately also determine which decisions are taken”.

Therefore, it can be understood that according to Healey (2003a), the quality of decisions being taken by directors does not rely solely on their aptitudes in adopting the right course of action, but also to which extent these resolutions is congruent to the long term goals of shareholders. This conflict of interest and other theories relating to the relationship among these participants in the governance system will be documented below.

2.2.Theoretical Background

It is a fact that the objectives pursued by shareholders and corporate managers tend to be differing and contradictory with regards to their own interests. Consequently, this has nurtured the conception of a wide spectrum of approaches and processes ensuring that conflicting interest' spill-over are minimized. One of the compromises that have been given birth to address this divergence is corporate governance. At its very root, according to some researchers (Harris and Raviv, 2008, Larcker, Richardson and Tuna, 2007) the theoretical platform on which foundations of corporate governance is built is weak and as such finds itself deprived of any theoretical base. Tricker (2000) and Parum (2005) also have the same line of reasoning and conclude that studies carried out on corporate governance have not been consistent whether empirically, methodologically, or even theoretically.

As such, a vast number of theoretical frameworks have seen the day, stemming from the fields of economics, finance, management or even sociology, so as to serve as a basis for researchers in their analysis of CG. Though to some (for instance Stiles and Taylor 2002), these piecemeal attempts to understanding CG leave them skeptic about the actual function of the BOD in a company, others like Solomon and Solomon (2004) have adopted an optimistic position and consider that these differing frameworks share commonalities on a theoretical base. The well known and widely discussed theories are the Agency cost theory (interested readers are referred to Berle and Means, 1932; Jensen and Meckling 1976), the Stakeholder theory (see Freeman et al., 2004; Kiel and Nicholson, 2003b; John and Senbet 1998); the stewardship theory (Donaldson, 1990; Pfeffer, 1972) and the resource dependency (see Ruigrok et al., 2006).

2.3.Empirical Literature

2.3.1.Conformance and Performance Issues

It is to be noted that notwithstanding the numerous theories that have been used as an approach to CG, there are two main principles that prevail and are continuously been applied. These are conformance issues (relating to directors' obligations) and performance issues. Both need to be balanced to maximize the chance of business success. The conformance dimension concentrate on an implementation of a regulatory model of operation for directors and concerns issues like board structures and their roles for instance. Conversely, the performance

issues encourage strategic value and promote the key drivers of performance.

In the early 1990s, there was evidence that CG was being induced fundamentally by conformance issues as BOD seeks to uphold their mechanisms as propounded by Francis (1997). However in the mid-1990's, Bosch (1995) and Hilmer (1993) have come to the view that too much focus was put on conformance issues to the detriment of performance dimensions and noticed the failure of CG processes to act as a catalyst for performance.

2.3.2. Corporate Governance Disclosures Effect on Firm Performance

The literature carries mixed results concerning the association between corporate governance and financial performance. Klapper and Love (2004) found a high positive association between better governance and operating performance using firm level data of 14 emerging stock markets with return on assets as a proxy for operating performance, although affirming that this may vary among countries. Likewise, some other researchers (Gompers et al. 2001, Drobetz et al. 2004, Brown and Caylor 2004) reported a positive relationship between the quality of CG and their measures of profitability.

Also, there is international evidence suggesting this positive link on certain developed markets. For instance, Selvaggi and Upton (2008) claimed that good CG enhances firm's performance for the United Kingdom and found the presence of a strong causality between the two variables. Similarly, Black (2001) reported the same conclusions in the case of Russian firms. In contrast, other studies reported no significant positive relationship between operating performance and CG. For instance, Bauer et al. (2004) argued that initially an insignificant relationship was reported which afterwards turned to a significantly and statistically negative relationship. A similar outcome was also observed by Beiner et al. (2004). Moreover, other studies (see Park & Shin 2004 and Prevost et al. 2002) did not found any evidence of any relationship between the two variables.

2.3.3.Board Effectiveness

Under the umbrella of board effectiveness, lie several factors but empirical studies have made use of board structure and composition with size, independence and performance as the key parameters. A board of limited size is expected to be more performing than bigger ones due to better communication and decision making thus improving performance. However, this consensus has not been reached unanimously as Brown and Caylor (2004) suggest a positive link while Beiner et al. (2004) suggest an insignificant association. But it is argued that efficiency goes concurrently with independence of board as evidenced by some authors in their studies while others (Haniffa and Hudaib 2006) have documented that

multiple directorship does not have a positive impact on performance.

2.3.4.CEO Duality

Rechner and Dalton (1991) concluded that firms with independent leadership outperformed those practicing CEO duality. However, Daily and Dalton (1992) reported a neutral finding with no relationship with operating performance.

2.3.5.Directors Remuneration

The general belief upheld is that higher levels of managerial compensation will encourage directors to perform their role more effectively. Though higher performance is expected, the findings are not conclusive as some (Canyon and Schwalbac 2000) have found the existence of such a relationship while others have failed to find empirical support for such a relationship. For instance, Duffhues and Kabir (2008) argued that this predominant insight of a link between the two variables doesn't always hold good as they did not report any significant relationship between executive pay and corporate performance.

2.3.6. Audit Quality

It is widely accepted that there exists a conventional wisdom that a higher quality level of audit forms part of a good governance mechanism. Indeed, auditors and audit committee play a crucial role in overseeing financial management of the company improving performance consequently. Most empirical works (Ho 2005) carried out have revealed positive findings whilst some, like Brown and Caylor (2004), have concluded that although there is a link between audit quality, governance and financial performance, the significance of the relationship lies between audit quality and dividend yield and not with operating performance!

2.3.7.Transparency and Disclosure

Greater disclosure and transparency enhance the reliability of financial information reported, closing the gap on information asymmetry and leading to higher quality of earnings forecasts by investors. Based on the premise that better corporate disclosure and transparency lead to better performance, Loh (2002) unraveled a list of potential benefits springing from higher level of transparency. This not only leads to better corporate performance but increases management trustworthiness, widens the investors' base and improves access to capital.

2.3.8.Social Responsibility

Corporate social responsibility is becoming a growing need of any organisations as they find them having a level of interaction between different stakeholders and with the society at large. Consequently, ethical behaviour on their part would send the correct signal to the different stakeholders and impact on performance. For

instance, Ho (2005) depicted in his survey a better performance standard than for firms without these fundamentals.

2.4. Scoring Corporate Governance Practices

Basically, each survey possesses its own way of constructing CG scores as it is contingent on the researcher's approach. Most part of researches done in this field of study, have focussed on available ratings constructed by several rating agencies. For instance, Klapper and Love (2004) made use of Credit Lyonnais Securities Asia to build up their governance indices while Brown and Caylor (2004) adopted the Institutional Shareholder Services database and alongside the application of Deminor ratings by Bauer et al. (2004). However, these ratings are usually in the ogle of institutional debate as they are sometimes argued not to be related with performance or, if so, only to limited extent due to significant factors being overlooked, thereby encouraging construction of own indexes. Essentially, Drobetz et al. (2004) computed their rating according to responses obtained from their surveys and added that to maintain transparency alongside interpretation, equal weighting was used across the different proxies. Similarly, Beiner et al. (2004) and Campos et al. (2002) in their construction of the rating, made reference to the underlying country's Code of Corporate Governance and OECD's (1999) Principles of Corporate Governance. Therefore, the scoring of CG is subjective, particular to the researcher and country and that is why the present study will attempt to construct a suitable index for the purposes of this survey.

2.4.1. Proxies for Financial Performance

Given the fact that measures used to capture the essentials of financial performance differ across studies, this underlines that there is no agreed consensus on which proxy is the best. For instance, Larcker et al. (2007) argued that return on assets "is likely to remove the impact of governance that we are trying to estimate" if "governance structures are stable over time" whilst others disagree on whether Tobin Q is a good approximate for firm value. In the light of the above, it is to be noted that there exists from the literature an extensive list of proxies adopted or models to estimate performance. However, one of the widely used composite measures of performance is Taffler's z-score model (1977) whereby calculations are based on several financial ratios being weighted and aggregated. Compared to the conventional ratio analysis, the z-score model discriminates financially healthy firms from those bearing a risk of potential failure.

3. Research Methodology

A cross sectional approach has been used which illustrate a specific situation and occurrence at a particular point of time being in 2008. Indeed companies' extent of compliance with CG practices and its link with their

performances will be evaluated over this period. The Companies which have been selected for assessment of CG for the present study are the top 100 companies in Mauritius as at 2009, ranked by "Business Magazine" according to their annual profit. For the proposed study, primary data was collected using a checklist as the research instrument, with sources of information for this assessment being the companies' annual reports whereby information about CG was readily accessible. The different sections enumerated on the checklist address issues on CG practices with regards to the proposed model designed in the conceptual framework discussed below. The data gathered from the annual reports for the purpose of the checklist were of various forms ranging from quantitative like the number of independent directors or number of shares held by each director, to categorical concerning the presence of a disclosure like list of shareholders holding more than 5% of the company, and ending with qualitative data extraction involving the scoring of the CG practices based on wordings in the annual report suggesting compliance is being achieved. As for the figures necessary for the computation of the Z-score, proxy for firm performance, these were gathered again from the companies' annual reports.

3.1. Sampling Techniques

Surveying the whole population is not only unrealistic but also unfeasible. As such, non-probability sampling was more apt to suit the data collection and analysis skills, more precisely judgmental sampling. The latter was more suitable since it enables the researcher to focus on the sample which suits his study. In fact, the top 100 companies selected, guaranteed assurance of those firms with highest performance with sufficient disclosures regarding best practice recommendations of CG. Then, the underlying sample was broken down into 3 groups representativeness of the sample being top 20

companies, 20 middle ones and 20 last companies to facilitate analysis and interpretation.

3.2. Conceptual framework of Corporate Governance used

While scrutinizing the different approaches and models used in the literature, and like some authors (Campos et al. 2002, Black et al. 2004), a conceptual framework has been developed based on the Mauritian CG. Thus the conceptual model has been developed wrapping 13 aspects in the checklist but classified under 9 factors for analysis as depicted by figure below and to mitigate the element of subjectivity, various elements of CG practices have been included covering a large number of questions as shown in table hereafter. Thus, it can be argued that the measures used are strong proxies and the factors constituting the checklist have been the most important ones as per previous literature while encompassing all aspects of CG. Concerning the scoring of the quality of CG, the same position as that of the World Bank survey on Mauritian listed firms has been adopted as shown in Appendix 1.

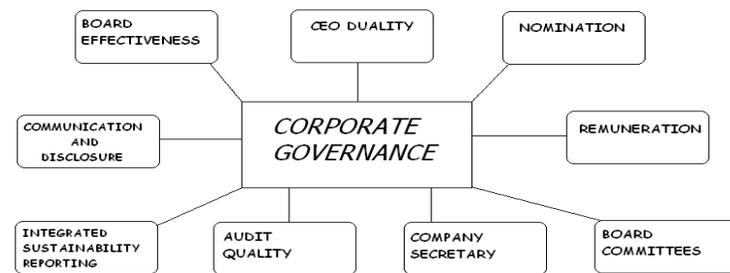


Figure1: Conceptual Framework

Table 1: Sub-Indices Questions

Sub-index	Questions
Board Effectiveness	1-6,15
CEO Duality	7-10
Nomination	11-14
Remuneration	16-19
Board Committees	20-23
Company Secretary	24-26
Audit Quality	27-34
Integrated Sustainability Reporting	35-39
Communication & Disclosure	40-51

accounting or market based performance measures have not gained consensus due to divergences in results. The

3.3. Proxy for performance used

The measure used to proxy performance is the Z-score adapted from Taffler model because the use of only

model is as follows:

$$Z = \sum_{i=1}^4 w_i \cdot x_i$$

Table 2: Methodology of Taffler model

Parameter	Weight	Calculation
X ₁	0.53	$\frac{EBT}{\text{Short - term payables}}$
X ₂	0.13	$\frac{\text{Short - term assets}}{\text{Short - term payables}}$
X ₃	0.18	$\frac{\text{Short - term payables}}{\text{Assets}}$
X ₄	0.16	$\frac{\text{Revenues}}{\text{Assets}}$
Z _T	Z _T > 0.3 Z _T < 0.2	financially stable company threat of bankruptcy

3.4. Univariate analysis

This was used to gain an insight into the data by presenting the individual variables constituting the CG framework through their mean and standard deviation according to the three categories of companies. The mean score was classified into “not observed”, “partially observed” and “observed” based on different scales depending upon the number of questions per determinant factor of CG. It is to be noted that according to Ho (2005), assessing the individual determinants of CG may not allow a full insight of the effect of CG as much as all the dimensions in unison. As such, a pie chart was used to represent not only the three levels of compliance of governance standards but also the three level of performance too, based on all companies surveyed to grasp a brief overview of the situation. Tests of normality, homogeneity of variance, independence, test of association and that of correlation were performed and nothing abnormal was to be noted

3.5. Regression Equations

Regression analysis allows the prediction of an outcome variable from one predictor variable and this will be analyzed through a simple regression as depicted by equation (1) below alongside the testing of the hypotheses deduced from the ANOVA shown in (2).

$$(1) Z\text{-Score} = \beta_0 + \beta_1 \text{Gov-Score} + \varepsilon$$

(2) H₀: The regression model can be used to predict the change in Z-Score

H₁: The regression model cannot be used to predict the change in Z-Score

4. Analysis And Discussion

4.1. Corporate Governance Score

Aggregating the nine factors from the conceptualized model, constituting the provisions of the Code of Corporate Governance, the CG score was constructed. Graphically, it is encouraging to note that above 50% of the sample has excellent CG framework in place covering the various issues and thus most companies are implementing the requirements of the Code. Moreover, 35% of the companies surveyed depict clearly the enthusiasm and the companies' commitment towards the upholding of the wide spectrum of provisions under the umbrella of our National Code of Corporate Governance. However, though not being hefty with 10% only, there are still some companies, all found in the bottom 20%, lagging behind in the pursuance of their compliance with much improvement needed to meet the intent of CG practices.

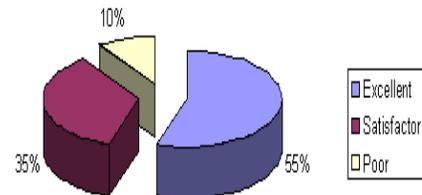


Figure 2 : Corporate Governance Score Categorical Analysis

Firm Performance (Z-Score)

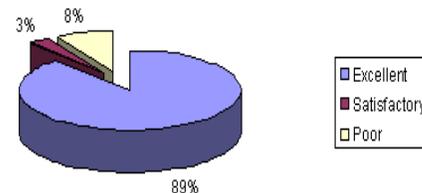


Figure 3 : Z-Score Categorical Analysis

Pooling together all the figures relating to performance across the three samples, an astonishing result has been yielded. Indeed, almost all companies have got excellent performance with no danger of bankruptcy surrounding them. This is remarkable in the sense that the financial crisis has not engulfed their profitability levels according to the Taffler model, which means no specific adjustment has to be done to account for this particular phenomenon and besides this low 8% poor performing companies stipulates that companies found in the bottom half of the top 100 list are not to be viewed as having low operating performance due to their reduced size and scale of activities.

4.3. Corporate Governance & Firm Performance Test of Association: Top 20 Companies

Table 3: Cross Tabulation of Gov-Score and Z-Score for top 20 companies

		Z-Score			Total	Percentage
		Poor	Satisfactory	Excellent		
Gov-Score	Poor	0	0	0	0	0%
	Satisfactory	2	0	0	2	10%
	Excellent	0	1	17	18	90%
	Total	2	1	17	20	100%
Percentage		10%	5%	85%	100%	

A hefty 90% of the top 20 companies have made it a must to ensure compliance with the CG principles which indicate clearly a real concern for the best firms to be viewed as having a high quality of CG so essential to their activities and to their surroundings. In fact, these had important repercussions on their performances as out of the 90% (n=18), 17 had achieved performance of high

standard, which may leave us to presume the vital role played by efficient boards among others. Concerning the other 10%, they have registered satisfactory governance score implying they have limit themselves to compliance of the main provisions and it is astonishing to see that those 2 companies have seen their profitability at low levels announcing imminent or eventual risk of facing bankruptcy

Table 4: Chi-Square Test for top 20 companies

Statistic	Sig.	Interpretation
Pearson Chi-Square	0.000	Evidence of association
Likelihood Ratio	0.002	Evidence of association
Linear-by-Linear Association	0.000	Evidence of association

It is apparent and clear that the chi-square test does not place reliance on assumptions of normality of data as the categorical data are not by nature continuous but however it has got nevertheless 2 important underlying assumptions. The first one has been fulfilled as depicted by the test of independence carried out previously whereby the independence of data has been found. The second assumption requires that all expected frequencies should be greater than 5 but however in the present case 5 cells have had expected count less than 5 with the

smallest expected count being 0.10 which reveals a loss in statistical power. Nonetheless, as can be inferred by the above test the test has not fail to detect a genuine effect as the value of the chi-square statistic is highly significant (p-value < 0.001) suggesting and implying that the type of CG framework adopted by a company had a significant effect on whether the company would perform better or not. The likelihood ratio and the linear-by-linear association statistics confirm the main chi-square result of an evidence of an association between CG and firm performance.

Table 5 : Cramer's V for top 20 companies

Statistic	Value	Sig.	Interpretation
Cramer's V	1.000	0.000	Evidence of a very strong association

Since there has been evidence of an association, we can proceed further to test the strength of the association between the two variables through the Cramer's V. It can be noticed that an extremely strong association exists between the CG quality and the firm performance as out of a possible maximum value of 1, the Cramer's statistic

has yielded 1 which is dumbfounding as results. Nevertheless, this value cannot be said to have occurred by pure chance as it is highly significant with a p-value being less than 1%, depicting and reaffirming again that the relationship is significant.

Middle 20 Companies

Table 6: Cross Tabulation of Gov-Score and Z-Score for middle 20 companies

		Z-Score			Total	Percentage
		Poor	Satisfactory	Excellent		
Gov-Score	Poor	0	0	0	0	0%
	Satisfactory	0	0	9	9	45%
	Excellent	1	0	10	11	55%
	Total	1	0	19	20	100%
Percentage		5%	0%	95%	100%	

Out of the 45% (n=9) of the companies which did have satisfactory and acceptable levels of CG provisions, it has been observed from the table that all of them had experienced a healthy financial status which differs completely from the observations in the top 20 companies. As such, those companies that were gauging the same extent of CG had found themselves in poor financial conditions. Besides, the remaining 55% allows

us to contemplate the likelihood of an eventual relationship as excellent CG are taking the companies to high levels, except for one company which seems to be an anomaly but a closer look at that company reveals that in ranking it in the top 100, sufficient attention had not geared towards the extraordinary item present, being surplus on portfolio investments hiking its profits up and classifying it among the best performing companies.

Table 7: Chi-Square Test for middle 20 companies

Statistic	Sig.	Interpretation
Pearson Chi-Square	0.353	No evidence of association
Likelihood Ratio	0.266	No evidence of association
Linear-by-Linear Association	0.366	No evidence of association

From the above table we can notice that all statistics are pointing at the acceptance of the null hypothesis, which is testifies that there is no association between CG practices and the level of performance as can be depicted by the insignificance of the values of the different statistics

though 2 cells only have had expected count less than 5. Thus, for middle 20 companies, the differing cultures adopted towards CG principles seem to have no effect on operating performance and the 'why' will be discussed later and since there is no association, the Cramer's V test will not be applicable.

Bottom 20 Companies

Table 8: Cross Tabulation of Gov-Score and Z-Score for bottom 20 companies

		Z-Score			Total	Percentage
		Poor	Satisfactory	Excellent		
Gov-Score	Poor	1	0	5	6	30%
	Satisfactory	0	0	10	10	50%
	Excellent	1	1	2	4	20%
	Total	2	1	17	20	100%
Percentage		10%	5%	85%	100%	

Indeed, some important observations can be drawn out based on the cross tabs. For instance, out of 50% of the companies having minimal compliance with CG provisions, all of them excel in their respective field of

activities. But what is most alarming is that out of the 30% (n=6) having neglected the importance of the Code of CG, 5 had achieved very honorable performance level which suggests that having a poor CG framework does not adversely affect the profitability of the company.

Table 9: Chi-Square Test for bottom 20 companies

Statistic	Sig.	Interpretation
Pearson Chi-Square	0.135	No evidence of association
Likelihood Ratio	0.136	No evidence of association
Linear-by-Linear Association	0.453	No evidence of association

The highly insignificant result represented by a p-value exceeding the 5% significance level, indicates that there is no association between the CG of the firm and the consequent performance levels attained by the companies which perhaps may have been exacerbated by the loss in statistical power experienced, depicted by the footnote showing the violation of the 2nd assumption

through 7 cells having expected count less than 5. Nevertheless, the pattern of governance and performance standards is significantly not different, as 85% of the companies had excellent performance levels despite varying degrees of CG score. Also, it is to be noted that the Cramer's V will not again serve any purpose in this situation of no association.

Correlations: Top 20 Companies

Table 10 : Correlations for top 20 companies

Correlation Coefficient	Sig.	Interpretation
0.714	0.000	Evidence of positive correlation

Given the fact that the data has violated parametric assumptions, the Spearman's rho, a non-parametric test has been used to measure the interrelationship between the two variables. The correlation coefficient enables the quantifying of the strength of the relationship between two variables. From the above table, it is clear that the coefficient indicates a strong positive relationship, meaning that both variables will move in the same direction, that is higher governance scores will generally be associated with higher z-scores and the reverse is also

true. This is in truth in unison with our findings reported under the chi-square test and on top of that the result is significant even at 1% significance level, reducing the probability that such relationship has been established by luck. Moreover, deriving the coefficient of determination through r^2 , $(0.714)^2$, we can affirm that the Z-Score can account for approximately 51% of the variation in the governance score though being highly correlated, leaving the other 49% of the variability still to be accounted for by other variables.

Middle 20 Companies

Table 11: Correlations for middle 20 companies

Correlation Coefficient	Sig.	Interpretation
-0.061	0.799	Evidence of negative correlation

Concerning the middle slice of the top 100 companies, a very weak negative relationship can be reported based on the above table, meaning that lower governance scores will be associated with a slightly higher performance levels but however the significance value being greater than 0.05 suggests that this relationship

may not hold good and that in fact the two variables may be simply independent. Computing the coefficient of determination, $(-0.061)^2$, it can be concluded that 0.37% only of variation is accounted for the Z-Score in the governance score meaning that the relationship seems almost to be trivial as if having no underlying theory.

Bottom 20 Companies

Table 12: Correlations for bottom 20 companies

Correlation Coefficient	Sig.	Interpretation
0.428	0.060	Evidence of positive correlation

As for the bottom 20, there is evidence of an almost weak positive correlation meaning that higher governance scores will lead to higher operating performance but however the p-value is just above 0.05 reducing confidence in such a relationship and ascertaining the absence of such genuine relationship between the two variables. The coefficient of determination, (0.0428) ², reveals that in this model the Z-Score can account for 18.31% of variation in the governance score revealing the presence of other independent variables to explain statistically the 81.69% variation of the dependent variable. Thus to enable us to have a clearer picture of the actual overall situation given the divergence of results, a simple regression analysis will be used to settle this issue.

Regression Results

Table 13: Regression Results

Model Summary ^b

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Change Statistics					Durbin-Watson
					R Square Change	F Change	df1	df2	Sig. F Change	
1	.447 ^a	.022	.005	15.20773	.022	1.281	1	58	.262	2.021

^a. Predictors: (Constant), GovScore

^b. Dependent Variable: ZScore

ANOVA ^b

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	296.318	1	296.318	1.281	.262 ^a
	Residual	13413.946	58	231.275		
	Total	13710.264	59			

^a. Predictors: (Constant), GovScore

^b. Dependent Variable: ZScore

Coefficients ^a

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	-6.657	9.585		-.695	.490
	GovScore	.071	.063	.147	1.132	.262

^a. Dependent Variable: ZScore

To establish whether a linear relationship in fact exists between Gov-Score and Z-Score, a simple regression has been used to capture the overall fit of the model illustrated below.

$$Z\text{-Score} = \beta_0 + \beta_1 \text{Gov-Score} + \epsilon$$

Based on the results of table 13, it can be outlined that R has a value of 0.147 and since there is only one explanatory variable, this value portrays a simple correlation between CG and firm performance. However the null hypothesis of β_1 being different from zero has been rejected since the observed significance is greater than 0.05. Moreover, the value of R² is very low and stands at 0.022 meaning that the governance score can only account for 2.2% in Z-Score variation which indicates the presence of other more relevant factors explaining this variation. In fact, if we generalize the model, things get exacerbated as definitely no relationship is seen between the two variables represented by the extremely low adjusted R². Also, it is worth noted that the Durbin Watson statistic is in the vicinity of 2 indicating the absence of autocorrelation which could have affected our model by inflating R² and making the model looks better than it was. The ANOVA lets us know whether the overall regression model can act as a good predictor of the outcome variable. Indeed it can be seen that the value representing the gradient of the regression line is 0.071, meaning that if Gov-Score is increased by one unit, performance level (Z-Score) will increase by an insignificant 0.071. However, this does not seem to reflect the genuine effect since the F-Value is very low and the p-value is not significant at the 5% level and thus the model is not a good predictor of firm performance.

4.3 Reasons for absence of relationship

-The final draft of the provisions of the Code of Corporate Governance for Mauritius has seen the day in 2004 and one cannot create a legitimate expectation to adopt this type of behavior overnight. Sufficient bridging space has

to be given for the companies to accommodate to this new framework and change their internal systems and conduct of businesses. As such, compliance has not been met at the highest level but this does not mean that these transitional provisions will affect the performance levels in a jiffy. Indeed, before the implementation of the Code, have the companies with their own internal systems put in place been always bankrupt and unprofitable? Of course the answer is no and thus the lack of relationship can be understood as another culture has been present to ensure profitability at high levels. This is concurrent with the argument of Roche (2005) who considers that an extended time period is a sine qua non to observe the influence of CG on shareholder value.

-To be seen as being compliant with the governance standards may be seen as a way to lure investors in financing their projects and investing massively in their businesses without in fact imbibing the governance provisions in their day to day activities. The aftermath will be an upsurge in operating performance without any consequential amendment to their 'actual' level of compliance.

-For listed companies on the SEM and DEM market, alongside commercial banks, there are usually stringent rules already in place so that the introduction of the governance provisions may have been adopted just for the sake of compliance with the Code to ensure their special positions of trust is maintained. This entwines with Roche (2005) suggestion that legal roots of the country will send corporate governance out of the limelight in impacting on performance.

-Following the reasoning of Klapper and Love (2002) that good CG practices will be more high-priced in countries where investor protection is sub-standard, we can deduce that Mauritius possessing appropriate regulatory frameworks and high levels of investor protection allows firms to attract investors despite poor compliance levels.

-It has been remarkable to note that smaller companies constituting the bottom 20 companies are lagging behind in the implementation of the anchoring points of CG but this however does not hinder them from being lucrative. In almost all cases, the small entities form part of a large holding structure which possibly surveys their activities in such a way that non compliance with the CG practices will not prove to overshadow their good performance levels. This overlaps the conclusion reached by Haniffa and Hudaib (2006) that high ownership concentration through large holding companies help in boosting performance even with low CG principles.

-The data source may have played a great role in displaying such a relationship due to the fact that the annual reports may not have been a comprehensive and all encompassing list of compliance of CG standards for some companies or some may simply have not bothered themselves in disclosing their battery of efforts towards compliance with the governance provisions. Thus ipso facto, they may be complying and yielding higher profits

without us realizing this link and therefore future analysis calls forth for a wider span of collection of data.

-Indeed, though the systems and structures conducive for good governance practices are important, the ultimate success of the company lies in the hands of competent people and thus minimally compliant companies may indeed have an effective workforce.

-The issue of endogeneity may have distorted the reported findings as Agrawal and Knoeber (1996) have experienced whereby this led to no significant relationship between corporate governance variables and performance.

5. Conclusions and Recommendations

This study focused on a potential association between CG and firm performance between different categories in the first stance for the top 100 companies in Mauritius. We created a measure to proxy CG and tested it against another one designed for firm performance based on the Taffler's model. However, though a significant relationship has been documented for the top 20 category of companies, the other results were inconclusive.

The findings showing an overall satisfactory level of corporate governance quality, are consistent with the researches done on Mauritius, whereby the CG Unit of the World Bank documented that all the main principles were partially observed while Mahadeo and Soobaroyen(2009), under the aegis of the Mauritius Research Council showed that the implementation of the principles is in place. But the core of the study which involves mainly establishing a potential link between the two constructs has been unfruitful. In truth, contrary to the claims in the literature, the implementation of CG provisions in Mauritius does not contribute towards firm performance. This is so mainly because, the upholding of the principles is viewed by some as a mere procedural compliance while others comply in form not in substance.

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