The influence of corporate governance and ownership structure on the financial performance of Banks in the UK

Abstract

Aim: This article aims to determine the effect of corporate governance and ownership structure on the financial performance of Banks in the UK.

Design/Method: Quantitative methodology is assessed in this article and Stata was utilised as the tool for the assessment of the secondary data. In this manner, the GLS model has been carried out to determine the effect. Moreover, the data has been gathered considering 20 banks from 2011 to 2020 in the UK.

Findings/Results: The results developed through the method led to the comprehension that the board independence, board member affiliations, board structure type, board structure policy and board size influence ROE and ROA. The results deliver that the corporate governance and Ownership structure have a potential influence on the financial performance of Banks UK.

Keywords: *Corporate Governance, Ownership Structure, Firm Performance, ROA, ROE, UK.*

Introduction

Corporate governance (CG) is found as one of the most important aspects in contemporary times and most organisations grow and expand in both the ways like for developing and emerging economies (Cuomo et al. 2016). Companies tend to expand their all used raw material that employed within the local workforce, community sell, paying taxes, etc., which indirectly benefited the organisation. Moreover, consequences for a firm's failure tend to be very high and can be dealt with in every aspect of society. For instance, investors can directly be removed out the overnight, and job losses tend to occur. As per the study of Clarke (2016), corporate governance has been seen as the most indispensable element especially for market discipline and this directly helped for fuelling the demands especially for the strong level of corporate governance mechanism through the investors with the other participants of the financial markets. As most of the regulators have already enacted corporate governance reforms through law in many countries like USA and UK. As in a country like the UK, codes of corporate governance are principles and one of the best practises within some indirect element of the legislature operation by the respect of some respective stock exchange listing rules. In addition, it has been found that ownership structure increases by the time and most of the researchers had looked through the shareholder like managerial, institutional, concentrated along with the foreign, considered as the potential monitors just because to monitor advantage over the diffuse shareholders (Amin & Hamdan, 2018). As they are increasing with the shareholdings and their aim for maximizing their all return on investment and might create the new management discipline. Meanwhile, the ownership structure is closely connected through the conflicts that affect operating performance for the firm. It has been asserted by Kraakman (2017), that ownership structure usually leads towards conflict and such kind of conflict of interest tends to cause agency problems. As most of the organisations' ownership structures tend to change and ownership is directly separate from the control, along with the incentive alignment problems that become evident.

Therefore, the main purpose of this is to analyse empirically influence of corporate governance (CG) and Ownership structure on the financial performance of Banks in the UK. Hence, to achieve this aim following objectives have been designed.

- To demonstrate the significance of corporate governance and ownership structure on the financial performance of banks.
- To determine factors that influence the financial performance of the Banks in the UK.
- To examine the influence of corporate governance and ownership structure on the financial performance of Banks in the UK

Literature Review and Hypothesis development

As corporate governance (CG) tend to put more focus on the control system along with the structures through which managers are found to be accountable for the banks' legitimate stakeholder (Solomon, 2020). Hence, traditional financial literature indicated some of the mechanisms that help for solving the corporate governance (CG) problems. Moreover, interest of the stakeholders at the banks has been extended beyond the interest of the shareholders from the time bank depositors and the creditors and regulators have been at risk in the bank as well. Additionally, all the shareholders along with the managers, depositors and the regulators hold all straight kinds of stakes for the performance of the bank (Stulz, 2016). As borrowers had the more of the legitimate claim especially on the banks through entering for lending the agreements, as they acquire more power and urgency by the cause that has been adopted through the stakeholder like regulators and consumer firms. Meanwhile, these kinds of stakeholders tend to enjoy all kinds of attributes related to a stakeholder that is power, legitimacy and urgency. Moreover, government tend to be more worried about the banks' reputations and consequently regulate their governance level because a failure of the banks directly affects the country in a negative way on their economy and this spread on the global level (Almutairi & Quttainah, 2017).

Furthermore, ownership structure directly indicates the types along with the composition of a shareholder in the organisation. However, it has been noted that control found to be as the important exchange term with the ownership as there are also other items like pyramids of the ownership, rights for the voting, and some different kinds of shares that had to be considered with this regard (Dan-Cohen, 2016). However, it has been further discussed in the study of Wood & Jones (2016) that bank ownership structure might fluctuate through having just a few owners for having a wide and more diversified level of stakeholders. Most of the banks tend to manage by controlling the individuals, where some other banks hire independent managers for the operations of their banks. Hence, each of these ownership and control relationships has a strong effect on the banks' performance.

Hypothesis 1: The board independence has a significant impact on the return on assets (ROA)

Hypothesis 2: The board Independence has a significant impact on the return on equity (ROE)

Most of the time, boards are usually composed of all executive and non-executive directors, as executive directors are known as the dependent directors and in other ways, non-executive directors refer to independent directors (Goh & Gupta, 2016). It has been discussed that at least one-third portion of the independent directors had to be presented in the board and just for the effective working board and especially for the monitoring, that is unbiased. However, Wang (2018) mentioned that dependent directors are considered to be one of the important aspects because they contain all the inside knowledge for the organisation that is not available for the outside directors, nevertheless, these dependent directors had a complete opportunity to misuse the knowledge by transferring values of stakeholders.

Hypothesis 3: The Board Member Affiliations has a significant impact on the return on asset (ROA)

Hypothesis 4: The Board Member Affiliations has a significant impact on the return on equity (ROE)

It has been found from the research conducted by Dasgupta et al. (2021) that most institutional investors have now perceived corporate governance as one of the important tools for extracting value for the shareholders that are underperforming and undervalued organisations. Furthermore, most of the target organisations that are found as underperforming and analyse their practices of corporate governance that directly lead towards the improvement that help for unlocking the hidden value of the organisation (Rebentisch & Prusak, 2017). Hence, such kind of improvement often includes replacing poorly performing directors that ensure about the organisations comply within perceiving best practise in the corporate governance. As it has been found that corporations with most of the active and independent boards appeared for performing much better than through the passive and non-independent boards. Hence, most of the investors tend to prepare for paying a premium investment in the organisation with some good corporate governance, as frequently scheduled meetings are directly generated opportunity costs that are in the form of time consumed by the management along with the cash costs in form of travelling allowances and fees for boards' members (Eisenhofer & Levin, 2019).

Hypothesis 5: The Board Structure Type has a significant impact on the return on asset (ROA)

Hypothesis 6: The Board Structure Type has a significant impact on the return on equity (ROE)

It has been found that right after the crisis in the global financial that hit the economy of the world in 2008, as most of the European banks has setter up different rules along with the regulations linked to corporate governance for improving the performance of their banks (Green, 2016). Hence, rules and the norms of corporate governance are one of the essential aspects for the economies of successful markets and European regions had provided their whole interest for improving corporate governance (CG) guidelines since the time until it shows a significant impact on the performance of a bank. Meanwhile, another study from the Mateus & Belhaj (2016) explained that there has been a major difference among the corporate governance in the European countries that are directly linked to the board structure and some of them use unitary systems and some use the two-tier system.

Hypothesis 7: The Board Structure Policy has a significant impact on the return on asset (ROA)

Hypothesis 8: The Board Structure Policy has a significant impact on the return on equity (ROE)

In addition to this, the effectiveness of the bank's internal governance is dependent on the detailed efficiency for their different elements, and notably about a count of directors who are on board, and percentage of the directors who are external along with the internal director's ownership, as well as the structure of meeting that held (Cheng et al. 2021). Meanwhile, as more of the details related to the criteria for some of the ideal choices especially for the members of board and found that a very high level of moral integrity along with professional competence, members had to be more trained according to the rules and regulations. A study conducted by Bidabad et al. (2017) mentioned that the board had to make sure some transparency that is sufficient for the disclosure of information that relates to the bank activities.

Hypothesis 9: The Board Size has a significant impact on the return on asset (ROA)

Hypothesis 10: The Board Size has a significant impact on the return on equity (ROE)

Large boards comprised of the more present directors in terms of quality and quantity, as different choices have been provided with more opportunities especially for the senior managers for making a selection of directors with more experience and some special expertise (Adams, 2017). However, size of the board helps to improve the reporting of governance and tend to influence the quality of the director oversight. Hence, Crifo et al. (2019) stated that some of the organisations found that organisations with huge boards provide a positive influence on the financial performance of the banks. Besides that, small boards are directly taken towards the creation of relationships, which are convicting and either by aligning interest for the executive with those of shareholders or just by aligning interest related to executives and directors.

Theoretical framework

Agency theory is one of the important aspects of corporate governance as it is considered the backbone for successful corporate governance policies and regulations (Alatassi & Letza, 2018). Especially in today's era where there has major collapse seen along with the debate related to strengthening the level of corporate governance and to make sure that it is more effective and efficient especially for protecting the interest of shareholders and some other stakeholders. Thus, agency theory tends to provide a basis for organisation governance by the use of a mechanism that is internal and external (Bosse & Phillips, 2016). Hence, the governance mechanism tends to design for protecting shareholder interests, and minimise the cost of agency and helping to ensure agent-principal interest alignment.

Conceptual framework

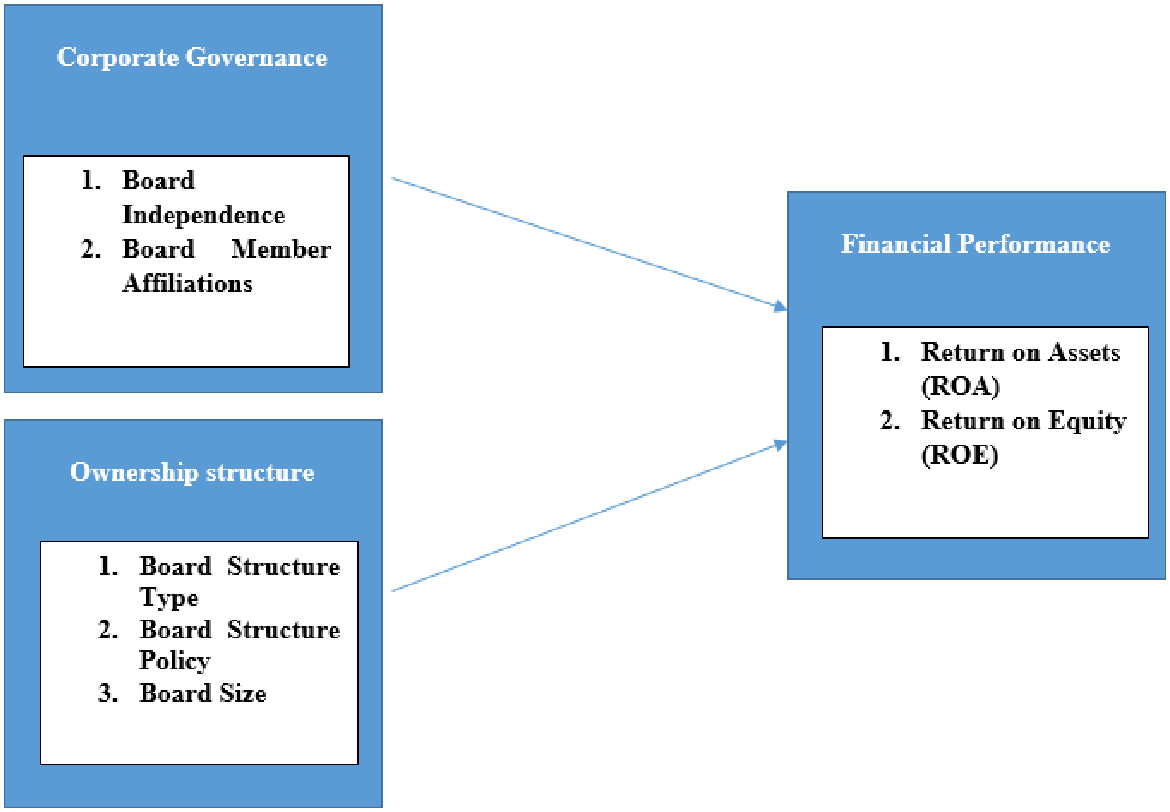

Figure 1 Conceptual Framework

Source : Author (2021)

As to conduct this study, the researcher use five variables as the independent variable, which includes board independence, board member affiliations, board structure type, board structure policy, and board size. However, to find the significant impact of these factors two dependent variables have been identified that are return on equity (ROE) and return on assets (ROA).

Methodology

In the current study, positivism approach has been used. As per the findings of Babones (2016) philosophy of positivism helps in providing a structure for the collection and analysis of data. The author further adds that utilisation of positivist approach can also help in mitigating the number of errors in research outcomes. In another study Babones (2016) indicate that positivism approach is based on the collection and interpretation of data, and reaching an effective conclusion. Therefore, positivist philosophy facilitates in ensuring the structure of the research process in the collection, analysis and interpretation of data, that overall improves the outcome of the research. Further, it also increases the authenticity and validity of the data.

In this research, a quantitative research design has been deployed that is based on the numbers and figures. The justification of using this method, as per the findings of Nardi (2015) it enables the researcher to collect numerical data about the factors that impact the financial performance of the banks in the UK. Moreover, quantitative research design also allows the reciprocity for future research (De Bruijne & Wijnant, 2014) therefore, the impact of quantitative research design and its outcome is another justification for using this method. Thus quantitative research designed significantly helped in analysing the elements that influence the financial performance of the banks.

According to (Choy, 2014) data can be collected in two ways primary data collection and secondary data collection. Chu and Ke (2017) in their study discussed that the primary data collection method is defined as the process to collect the data through using surveys, interviews, and observations. Whereas the secondary data collection method refers towards second-hand data that has been published and analysed in existing studies relevant to the research phenomenon. However, in the current research, a secondary data collection method has opted. The researcher acquired the data from Annual reports of the banks, Reuters, and morning star websites from 2011 to 2020. The primary reason for using this method is that it allows the researcher to collect in-depth information relevant to the research problem.

In the current research, the data that has been collected is secondary quantitative. Therefore, based on this justification correlation, and regression (random and fixed effect, and GLS model) has been used for the analysis. This analysis has been done by using Stata software.

The justification of using these methods, as in the study of Ryan (2018) indicated that correlation and regression analysis allows the researcher to recognise the association between dependent and dependent variables and reach on rational conclusion. Similarly, Arkkelin (2014) in their study adds that utilisation of Stata software can significantly help in the analysis and interpretation of the results that have been extracted from large complicated data sets. Therefore, based on this justification Stata has been used, and it has significantly helped in analysing the factors that influence the financial performance of the banks.

Analysis

Descriptive Analysis

The research of Sidel, Bleibaum and Tao (2018) comprehended that the descriptive analysis is a potentially significant part of the research as the brief description coefficients result in the summarization of provided data set which develops the opportunity of the representation of the entire population which is being tested or a specific sample of the population. In addition to this, another study that discussed the significance of descriptive analysis led to the development of the conclusive idea that descriptive statistics are further divided into measures of the central tendency as well as that of variability (Kemp, Hort & Hollowood, 2018). The descriptive statistics which is carried out in this research delivers a variety of the assessed measure, out of which, mean and standard deviation, are considered as significantly considerable for the development of results.

Table 1 Descriptive Statistics

Variable	Obs	Mean	Std.Dev.	Min	Max
ROA	200	0.092	0.147	-0.430	0.779
ROE	200	0.130	0.268	-1.637	1.120
Board Independence	200	0.722	0.172	0.000	1.000
Board Member Affiliations	200	0.896	0.723	0.000	3.818
Board Structure Type	200	0.090	0.287	0.000	1.000
Board Structure Policy	200	0.950	0.218	0.000	1.000
Board Size	200	6.745	2.433	2.000	13.000

Table 1 which is included above demonstrates the mean value of independent variables. It shows that the mean value of independent variables. The mean value of ROA is 0.092 displaying a low accumulated variety of the generation of ROA in companies. It further delivers that the mean of ROE is 0.130 showing that most firms have significant ROE generations in the company. In addition to this, Board Independence, Board Member Affiliations and Board Structure Type are found to have means of 0.722, 0.896, 0.090 and 0.950 respectively. Whereas, the Board size shows a large means of 6.745 which comprehends the way the companies have large structures. From Table 1, it is further observed that std. dev. Of ROA is 0.147, std. dev. of ROE is 0.268, std. dev. of Board Independence is 0.172, std. dev. of Board Member Affiliations is 0.723, std. dev. of Board Structure Type is 0.287, std. dev. of Board Structure Policy is 0.862 and lastly std. dev. of Board Size is 2.433. It has been observed the mean value of standard deviation is inclined to a far lesser value than the mean.

Correlation

Correlation analysis is another method of assessment that is found to be significant in the light of the research subject. According to the study of Akoglu (2018), it is the method of evaluation of a simplistic association that is observed between variables included in the research.

Table 2 Correlation

	ROA	ROE	Board Independence	Board Member Affiliations	Board Structure Type	Board Structure Policy	Board Size
ROA	1						
ROE	0.6441	1					
Board Independence	0.0014	-0.024	1				
Board Member Affiliations	0.0368	0.013	-0.02	1			
Board Structure Type	-0.1102	-0.068	-0.12	0.0241	1		
Board Structure Policy	-0.1001	0.086	-0.07	-0.0105	-0.0882	1	
Board Size	-0.147	-0.085	0.057	0.2293	-0.0461	0.0326	1

The aforementioned table delivers the comprehension of the result of correlation of the variables which were assessed in this study. Concerning the ROA, the value of correlation presented by Board Independence is 0.001 showing no significant relationship between the two, Board Member Affiliations is 0.036 which represent the existence of no correlation, Board Structure Type is 0.110 which delivers no significant relationship, Board Structure Policy is 0.100 showing insignificant association and Board Size is -0.147 that shows insignificant of the relationship.

In relevance to ROE, the value of correlation of Board Independence is -0.024 which represents an insignificant relation between these variables, Board Member Affiliations is 0.013 which represents that no correlation exists among the two assessed variables, Board Structure Type is -0.086 which delivers an insignificant relationship, Board Structure Policy is 0.086 showing no significance and Board Size is -0.085 that comprehends the insignificance of this relationship.

Generalised Least Square (GLS) for ROE

The decision of adopting the GLS model of regression for the development of knowledge regarding the collected data is driven by the Hausman value which results in the determination of the adoption of the autocorrelation method (Patrick, 2021). For this research, the value of Prob>chi2 is discovered to be 0.7565 due to which the GLS regression method has been adopted.

Table 3 – GLS for ROE

ROE	Coef.	Std. Err.	z	P>|z|	[95% Conf.	Interval]
Board Independence	***0.016	0.003	5.440	0.000	0.010	0.022
Board Member Affiliations	***0.010	0.003	3.510	0.000	0.004	0.016
Board Structure Type	***-0.034	0.004	-8.180	0.000	-0.042	-0.026
Board Structure Policy	*0.015	0.019	0.800	0.425	-0.021	0.051
Board Size	***-0.005	0.001	-4.320	0.000	-0.007	-0.003
_cons	***0.139	0.021	6.520	0.000	0.097	0.181
Wald chi2(5)	258.44				Prob > chi2	0
*Significant at 10%; **Significant at 5%; ***Significant at 1%						

Table 3 which delivers the results of this method of assessment led to the revelation that there is a significant effect of board independence over ROE as B is equal to 0.016 and p=0.000<0.01. The variable of Board Member Affiliations has a significant impact over ROE as B is equal to 0.010 and p value=0.000<0.01. The aforementioned result of the assessed variable of the Board Structure Type is likewise discovered to be negatively influential over ROE due to B being equal to -0.034 and p=0.000<0.05 as per the above table. Moreover, the variable of Board Structure Policy was discovered to have a weak influence over ROE as B is equal to 0.015 and p=0.425>0.1 which ensures that this has a significant positive impact on the firm's performance. On the other hand, there is a significant impact of Board Size over ROE as B is equal to -0.005 and p=0.000<0.01 which led to the comprehension of the negative nature of this impact on the dependent variable.

Generalised Least Square (GLS) for ROA

For the selection of appropriate use of analysis method, the Hausman value was observed significantly by the researcher as this according to the research presented by Patrick (2021), leads the process of determination of the adoption of the autocorrelation method. For this research, the value of Prob>chi2 is discovered to be 0.753 due to which the GLS regression method has been adopted.

Table 4 GLS for ROA

ROA	Coef.	Std. Err.	z	P>|z|	[95% Conf.	Interval]
Board Independence	*-0.010	0.060	-0.160	0.872	-0.127	0.107

Board Member Affiliations	*0.016	0.014	1.080	0.278	-0.013	0.044
Board Structure Type	**-0.067	0.036	-1.870	0.061	-0.137	0.003
Board Structure Policy	*-0.071	0.047	-1.530	0.126	-0.163	0.020
Board Size	***-0.010	0.004	-2.350	0.019	-0.018	-0.002
_cons	***0.226	0.071	3.210	0.001	0.088	0.365
Wald chi2(5)	11.040				Prob > chi2	0.051

*Significant at 10%; **Significant at 5%; ***Significant at 1%

Table 3 which delivers the results of this method of assessment led to the revelation that there is a significant but negative association of Board Independence over ROA as B is equal to -0.010 and p=0.872>0.1. Board Member Affiliations as it found to have a significant effect as B is equal to 0.016 and p=0.278>0.1. The aforementioned result of the assessed variable of the Board Structure Type is likewise discovered to have a positive significance over ROA due to the value of B being -0.067 and p=0.061>0.05 as per the above table. Similarly, the variable of Board Structure Policy was discovered to have a significant effect as the B is equal to -0.071 and p=0.126>0.1. On the other hand, the influence of Board Size is significant on the dependent variable of ROA as B is equal to -0.010 and p=0.019>0.01.

Discussion and Hypothesis Assessment Summary

Table 5 Hypothesis Summary

S.No.	Hypothesis	Status
1.	The board independence has a significant impact on the return on assets (ROA)	Accepted
2.	The board Independence has a significant impact on the return on equity (ROE)	Rejected
3.	The Board Member Affiliations has a significant impact on the return on asset (ROA)	Accepted
4.	The Board Member Affiliations has a significant impact on the return on equity (ROE)	Accepted
5.	The Board Structure Type has a significant impact on the return on asset (ROA)	Accepted
6.	The Board Structure Type has a significant impact on the return on equity (ROE)	Rejected
7.	The Board Structure Policy has a significant impact on the return on asset (ROA)	Accepted
8.	The Board Structure Policy has a significant impact on the return on equity (ROE)	Accepted
9.	The Board Size has a significant impact on the return on asset (ROA)	Rejected

10.	The Board Size has a significant impact on the return on equity (ROE)	Rejected

The aforementioned table included in this study delivers the hypothesis summary of the current research. The first hypothesis of the research was that board independence has a significant impact on the return on assets. In case of the second hypothesis which is focused on ROE, however, the findings of the research revealed that the value of this variable is found to be insignificant than the threshold level which is required as a result, the hypothesis was rejected. This is also affirmed by the research presented by García-Sánchez et al. (2019) which stated that the independence of the stakeholders in the Board results in the development of a high rate of financial benefit through generation of ROA. This means that when the board members are provided significant independence they play a vital role in the development of profitable returns of assets but leave no impact on the return of equity.

The result of third hypothesis which is assessed for the research showed an evaluation that is contradictory to the results of the second one as the Board Member Affiliations for ROA is found to have significant impacts. The fourth hypothesis of Board Member Affiliations shows significant results on ROE generation, the fifth hypothesis of Board Structure Type on ROA was comprehended to have significant results. Moreover, the sixth hypothesis of Board Structure Type was described to have an insignificant effect on ROE development in the firm. The research presented by Chowdhury, Rana and Azim (2019) comprehended contrastingly, as the author concluded that the organisational structure has a vital role in the appropriate development of profit from both ROA but not in case of ROE, which shows a partial impact on the performance. Furthermore, the exploration of hypothesis related to the Board Structure Policy is another aspect to the ROA which added depth to the research and the hypothesis assessment of this comprehended that there exists a significant relation variable in development of ROA but in case of firm performance through ROE, it comprehends to have an insignificant effect. Lastly, the assessment of the hypothesis of Board Size on the ROA is found to be insignificant for the overall performance as it has an insignificant impact on both ROE as well as ROA. Through this, it is verified that in the current research findings, Board Independence, Board Structure Type and Board Size were sub-factors that had partial results in terms of acceptance as part of the hypothesis of organisational performance. On the other hand, the results for the Board Member Affiliations and Board Structure Policy has an undeniable role in the determination of the performance of a company.

Conclusion

The focus of this research was on the examination of the role of corporate governance and Ownership structure in the determination of performance of the firm. The research discovered that a series of factors tend to have an impact on the performance of the firm, which was Board Member Affiliations and Board Structure Policy. The method used in the researcher was a secondary quantitative approach and the software of Stata was adopted for this. Correlation findings of the research revealed a significant association of board independence over ROA which partially affects a firm's performance, which means that it occurred as an impactful factor that needed to be managed for profitability. Board Member Affiliations was discovered to be another significant influencer as it results in the development of impactful progress of the firm development. Other than this, board structure type is partial whereas board policy is fully influential in the enhancement of the firm's performance. This led to the conclusion that the corporate governance and Ownership structure both play a vital role in the performance of a firm.

Future Implications

The scope of this research is to emphasise the corporate governance and Ownership structure impact on the performance of the firm. The findings of the research revealed that the major impact was of the Board Member Affiliations and Board Structure Policy on the determination of the firm performance. Considering the aforementioned finding, the research being discussed is crucial in the implementing of strategies for corporate governance and establishment of appropriate Board Structure Policies for the appropriate firm management to ensure performance.

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