

# The Relationship between Corporate Governance and Financial Performance in the UAE Exchange Market

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## Abstract

This study examines the effect of corporate governance on the financial performance of listed companies in the United Arab Emirates (UAE) financial exchange market. The governance mechanisms employed in this study are Board size (BS), Board independence (BI) and four audit committee's (AC) characteristics which include AC independence, financial experts in the committee, number of AC meetings held during the year, and the incentives received by the AC members. This Study uses all the public listed companies in the UAE financial exchange markets including Abu Dhabi Securities Exchange (ADX) and Dubai Financial Market (DFM). The secondary data for five years are used starting from 2016 to 2020. The data were analyzed using descriptive statistics, correlation and multiple regression analysis (MRA) with the aid of SPSS V26.0. The result shows that BI has been found to negatively affect firms' performance. AC meetings and financial experts' did not affect a firm's performance, while AC incentives and AC independence negatively affected firms' performance. This study is supposed to fill the gap of the lack in CG studies based on the fast-growing economy of the UAE. Besides, this research investigates the AC's characters' effect on firms' performance which was rarely covered in the literature.

## Keywords

Corporate Governance, Board Size, Board Independence, AC characteristics

## 1. Introduction

The board of directors and board committees are responsible for corporate governance, which balances individual, societal, and economic aims. The separation between company ownership and control, based on the mechanism by which firms are directed and controlled, gives rise to CG (Farhan, Obaid, and Azlan, 2017). The CG structure defines forth the rules and methods for making corporate decisions, as well as the distribution of rights and obligations among different participants in the company (the board, management, shareholders, and other stakeholders). It also offers the structure through which the company's objectives are determined, as well as the means of achieving and monitoring those objectives. As a result, CG is on track to increase long-term shareholder value by improving corporate performance and accountability while also considering the interests of other stakeholders. CG is a set of structures, processes, cultures, and systems that are used to set objectives, determine how to achieve them, and assess performance, as well as direct and control enterprises (Al-ahdal et al., 2020).

However, the primary goal of CG is to improve corporate performance and accountability in order to increase shareholder value while also protecting the interests of other stakeholders. As a result, it complements the need for a company to strike a balance between the need to increase shareholder wealth and the need to balance the pluralistic interests of all stakeholders. The board of directors is a crucial control and oversight mechanism for company activity (Ibrahim and Abdullahi, 2019). Thus, the different codes of CG that have been produced both nationally and internationally as guides to what constitutes "best practice" in supervision have highlighted board size, board independence, board gender diversity, board remuneration, and board financial expertise (Singh et al, 2018; Unite, Sullivan, & Shi, 2019).

Researchers have paid close attention to financial performance, particularly in accounting and strategic management. This is understandable; given financial performance has an impact on an organization's health and long-term survival. Financial performance is defined as an organization's efficient and effective use of resources to achieve its goals, resulting in a growth in stock price, sales, market share, profitability, earnings, and cash flows, as well as meeting the expectations of its many stakeholders (Ibrahim, M, 2015).

Board size, board independence, and board gender diversity are among the board structures that are thought to play a significant impact in corporate governance. Advising and monitoring are the two most significant tasks of the board of directors. As a result, the board of directors is regarded as an important CG mechanism for matching the interests of managers and other stakeholders in a company (Sanda, Mikailu, & Garba, 2010). The size of a board has an impact on the quality of deliberation among members and the board's capacity to make the best corporate decision (Lawal, 2012). As a result, determining the optimum board size is critical, as board size might reduce CG effectiveness beyond its ideal level. However, in the CG literature, defining an appropriate board size has been a continuing and contentious topic (Lawal, 2012). The importance of board size in achieving board effectiveness and enhanced company performance was also discovered (Kiel, & Nicholson, 2003).

External directors, it was further said, support good governance by contributing their talents, connections, and contacts to satisfy all stakeholders and assure the corporation's improved financial performance and long-term survival (Johnson, & Greening, 1999). In order to assist the board in achieving its goal and ensuring the company's success, it is critical to have an effective board of directors with an acceptable director composition (Al-Matari et al., 2012). Gender diversity on boards leads to a better grasp of the market, according to previous study. This is because gender diversity on boards of directors mirrors the diversity of customers and staff in the marketplace, boosting a company's competitive advantage (Unite, Sullivan, & Shi, 2019). Furthermore, board diversity fosters creativity and innovation in decision-making, which improves a company's long-term financial performance. Boards are concerned about having the correct composition in order to present a variety of viewpoints. Female board members will contribute various ideas to the boardroom, provoking vibrant boardroom conversations, and greater female presence on boards will provide some extra talents and perspectives that may not be available with all-male boards (Paniagua, Rivelles, & Sapena, 2018).

Some research revealed that CG has a positive and significant impact on firm financial performance (Boyle, & Jane, 2011; Yauri, Muhammad, & Kaoje, 2013), while others found that CG has a negative and significant impact on business financial performance (Boyle, & Jane, 2011; Yauri, Muhammad, & Kaoje, 2013). (Jegade, Akinlabi, & Soyebbo, 2013; Saini, & Singhania, 2018) Within the same study, some researchers discovered that some variables had a beneficial impact while others had a negative impact (Sanda, Mikailu, & Garba, 2010; Jegede, Akinlabi, & Soyebbo, 2013; Akpan, & Amran, 2014; Garba, & Abubakar, 2014; 19-24). Similarly, the majority of empirical studies looked at the influence of CG on financial performance focused on a specific industry. Financial services, food and beverages, consumer goods, and global corporations are just a few examples (Rahim, & Alam, 2014; Garko, 2016).

### **1.1. CG in UAE**

The UAE has adopted extensive economic regulations and laws to facilitate and control investments in order to sustain and protect investors. The UAE government has enacted the CG code, which applies to all publicly traded companies (Farhan, Obaid, and Azlan, 2017). By the end of 2009, the UAE Ministry of Economy announced the CG code in Ministerial Resolution No. (518) of 2009 (the MCGC), mandating its implementation by all companies listed on the financial markets by May 2010. (Minister of Economy, 2009, No. 518, Article 16). Corporations listed on the UAE's financial markets must comply with the extent of the MCGC judgment. The MCGC defines the board's makeup, responsibilities, salary, and selection procedure, as well as its independence. The MCGC further states that the board should establish two subcommittees: the AC and the nomination and remuneration committee. In addition to other requirements, the MCGC set the duties, the number of members, and the minimum number of meetings required for each committee. The MCGC explicitly says that all publicly traded firms must use the capital markets. The MCGC warns that if the corporation does not comply, sanctions would be enforced (Farhan, Obaid, and Azlan, 2017).

## **2. Literature Review**

### **2.1. The Concept of Corporate Governance**

CG has been characterized in a variety of ways by various authors. CG is interested in how all stakeholders in a company try to ensure that managers and other insiders adopt a structure that protects the stakeholders' interests

(Sanda, Mikailu, & Garba, 2010). A typical company has several owners who do not manage the company and managers who have no or little stake in the company. The free-condition dilemma associated with diffused equity ownership prevents any shareholder from taking unilateral action to shoulder the costs of monitoring the managers, who may pursue goals that are incompatible with the shareholders'. CG is a set of procedures (accounting standards and laws governing financial disclosure, CEO compensation, and the size and composition of corporate boards) and institutions (legal, economic, and social) designed to safeguard the interests of the corporation's owners (Puni& Anlesinya, 2019).

CG is also the system by which a company's board of directors establishes and works toward attaining objectives by separating ownership and control in an effective and efficient manner (Rahim, & Alam, 014). In addition, CG can be thought of as a set of mechanisms by which organizations operate when ownership and management are separated, as well as systems that offer investors in corporations with some protection in their investments (Karaye, Ishak, & Che-Adam, 2014). CG can be defined as a system by which firms are directed and managed in the best interests of the owners and investors with the goal of creating shareholder value and meeting the expectations of other stakeholders, based on the aforementioned definitions. CG often addresses topics such as how boards and CEOs are chosen, what mandates and obligations they have, and if shareholders have a right to vote on certain types of corporate decisions, and if so, what shape these shareholder rights take.

## **2.2. The Concept of Financial Performance**

Scholars have characterized financial performance in a variety of ways. Financial performance refers to a company's capacity to reduce operating costs, maximize asset utilization, and increase shareholder value. High performance demonstrates management effectiveness and efficiency in utilizing a company's resources, which helps the economy as a whole (Afrifa, and Tauringana, 2015 27). Financial performance was described as an organization's endeavor to accomplish its objectives or production effectiveness (Karaye, Ishak, & Che-Adam, 2014). Financial performance, on the other hand, is a measure of an organization's earnings, profits, and value appreciation, which is represented in the rise in share price (Abdulfattah et al., 2020). Financial performance can be measured at a single moment in time or across time. It can also be compared to similar enterprises in the same industry, or it can be used to aggregate industries or sectors. From the foregoing, financial performance is a measure of an organization's earnings, profits and appreciation in its value which are reflected by the rise in share price and the degree to which financial objectives are being met or has been accomplished.

## **2.3. Studies on the Impact of CG on Financial Performance**

The impact of CG on financial success has yielded conflicting outcomes in studies. According to certain studies, CG has a good impact on financial performance (Sheikh, Wang, and Khan, 2013; Aggarwal, 2013). Other research have discovered that CG has a negative impact on financial performance (Akdogan, & Boyacioglu, 2014; Muller et al, 2014). Certain researchers discovered mixed results, with some variables having a favorable impact and others having a detrimental impact within the same study (Gill, & Mathur, 2011; Ylmaz, 2018; Hussain, Ahmad, & Hassan, 2019). Another study looked at the influence of CG on the financial performance of 15 banks listed on the Amman Stock Exchange (ASE) in Jordan from 2007 to 2009. (Al-Manaseer et al, 2012). Board size, board composition, CEO status, and foreign ownership were used as CG indicators, while financial performance measures such as ROA, ROE, NPM, and EPS were utilized as financial performance indicators, and bank size was used as a control variable. For data analysis, descriptive statistics and multiple regression analysis were utilized. The findings show a favorable association between the number of outside board members, foreign ownership, and bank performance in Jordan, but a negative relationship between board size and the separation of the roles of CEO and chairman.

Shahwan and Fathalla study the role of intellectual capital (IC) as a mediator variable in the relationship between corporate governance (CG) practices and business performance (2020). The level of CG practices and the performance of IC were assessed using the value-added intellectual coefficient technique and the designated corporate governance index. Tobin's Q (TQ) and the operating efficiency ratio were used to assess the firm's performance. According to the data, the aggregate CG score has a significant positive impact on the IC and the two metrics of company performance (Shahwan, & Fathalla, 2020). The impact of the Malaysian Code on Corporate Governance (MCCG, 2007 and 2012) on the performance of Malaysian listed companies is investigated by Bhatt and Bhatt (2017). According to the agency

theory and resource dependency theories, businesses with good corporate governance outperform those with poor governance.

Furthermore, utilizing panel data from 2006 to 2011, the relationship between ownership structure, board structure, and financial performance of 311 listed companies on the Tehran Stock Exchange in Iran was investigated (Golmohammadi, Ranjdoost, & Cherati, 2012). Ownership and board structure features were represented by ownership concentration, board independence, board size, institutional share ratio, and CEO duality, while financial performance was measured by ROE. For data analysis, descriptive statistics, OLS, Fixed Effects, and Random Effects regressions were used. The findings show a favorable correlation between board size and board independence, but a negative correlation between institutional share ratio, CEO duality, and firm performance, as well as no significant correlation between ownership concentration and business performance. More specifically, the impact of board qualities on financial performance of 30 Pakistani banks was explored using panel data from 2007 to 2011. (Javed et al, 2013).

The number of directors, the presence of non-executive directors, the CEO duality, and the number of board committees were used as proxies for board size and structure, whereas ROA was used as a proxy for financial performance. Data analysis techniques included descriptive statistics and linear regression analysis. The findings show a positive association between the number of directors, non-executive directors, CEO duality, and the presence of women directors, as well as a negative relationship between the number of board committees and financial performance.

Similarly, using panel data for the years 2002–2003 and 2008–2009, the association between CG mechanisms and financial performance of 105 companies listed on the National Stock Exchange of India (NSE) was investigated (Gull, Saeed, & Abid. 2013; Varshney, Kaul, & Vasal, 2013). Firm size, leverage, type of company, industry, risk, ratio of R&D expenditure to sales, ratio of advertisement expenditure to sales, and ratio of PBDITA to sales were used as proxies for CG. Economic Value Added (EVA), Tobin's Q, ROA, and ROCE were used as financial performance measures, while firm size, leverage, type of company, industry, risk, ratio of R&D expenditure to sales, and ratio of PBDITA to sales were used as control variables. The analysis used pooled and random effects regressions, and the results show that board size has a significant positive relationship with financial performance, whereas the proportion of outside directors, the number of board meetings, and CEO duality all have a negative relationship with financial performance.

Queiri et al. (2021) investigate the relationship between specific board qualifications and ownership determinants and company performance on the Muscat Securities Market (MSM30). The study looked at how the size of the board of directors, the number of board meetings, and the ratio of independent board of directors, as well as the types of ownership concentration, influenced the company's financial performance. Their findings suggest that the attributes chosen for board members and ownership have an impact on the firm's success. The association between the amount of application of CG principles and the financial performance of companies listed on the Istanbul Stock Exchange (ISE) National 100 Index in Turkey for the fiscal year 2008 was also explored (Akdogan, & Boyacioglu, 2014). The application level of CG principles was measured using ROA, ROE, and stock return as proxies of financial performance, with business size, firm age, and leverage ratio serving as control variables.

The results show that there is a strong and positive association between CG and financial performance, as revealed by multiple hierarchical regressions analyses. In addition, throughout the period 2004-2012, the association between board qualities and financial success of 50 businesses listed on the Egyptian Stock Exchange was explored (Muller et al., 2014). Board independence, board meeting frequency, CEO duality, and director ownership were used as proxies for board composition, financial performance was measured with ROA, ROE, and Tobin's Q, and firm size, firm age, and firm leverage were used as control variables. The data was analyzed using descriptive statistics, Pearson correlation coefficient, and GLS random effect regression. The study's findings demonstrate that there is a favorable and significant link between CG and financial performance.

In a separate study, the impact of board characteristics on financial performance of firms listed on the London Stock Exchange (FTSE100 members, which are the first 100 largest and most traded companies) over the period 2010-2011 was explored (Muller et al., 2014). Corporate board characteristics variables included board size, board independence, percentage of foreign directors, average service, tenure, age, and percentage of women directors; board compensation

variables included chair remuneration, non-executive director remuneration, additional remuneration for board committee meetings, and fees paid in shares; and ROA was used as a proxy for financial performance.

Another study looked at the impact of board qualities on the financial performance of 40 Egyptian listed companies using panel data from 2008 to 2010. (Wahba, 2015). The CG factors were board composition (BCO) and CEO duality (DUL); financial performance indicators were ROE and Tobin's Q; and control variables were company size, firm age, financial leverage, and capital intensity. The study's findings show that CG has a considerable detrimental influence on financial success. Furthermore, the relationship between CG structure, leadership style perception, and financial performance of listed DMBs in Nigeria during the 2008-2009 financial crisis was investigated (Garba, T., & Abubakar, 2014).

Another study looked at the impact of CG on the financial performance of 67 companies listed on the Tehran Stock Exchange in Iran from 2006 to 2012. (Rostami, S., Rostami, Z., & Kohansal, 2016). Ownership concentration, institutional ownership, board independence, board size, CEO duality, and CEO tenure were utilized as proxies for CG, ROA, and stock returns as proxies for financial performance, and MVE and the ratio of book value to market value of the equity as control variables. The findings show that there is a considerable positive association between ROA and stock returns, as well as ownership concentration, board independence, CEO duality, and CEO tenure (Rostami, S., Rostami, Z., & Kohansal, 2016). Institutional ownership and board size, on the other hand, have a considerable negative association with both return on assets and stock return. Similarly, the CG practice and its association with financial performance of 86 of Bursa Malaysia's Top 100 public listed businesses from 2008 to 2012 were investigated (Zabri, Ahmad, & Wah, 2016). The CG factors were board size and board independence, whereas financial performance was examined using ROA and ROE. The findings demonstrate that board size has a weak negative association with ROA but is insignificant with ROE, and that board independence has a positive and negligible link with company performance (Zabri, Ahmad, & Wah, 2016).

In a further study (Ylmaz, 2018), the relationship between CG and financial performance of 61 companies trading on the Muscat Securities Market in Oman from 2013 to 2016 was explored. The CG score was employed as a proxy for CG, and financial performance was measured using Tobin's Q, return on asset, profit margin, EBIT margin, and net profit margin, with size gearing and firm growth as control factors. The data was analyzed using descriptive statistics and multiple regressions, and the results suggest that there is a positive and substantial association between CG and financial success of enterprises in Oman (Ylmaz, 2018). In comparison, the impact of CG on the performance of four multinational corporations in Nigeria from 2012 to 2016 was investigated (Akinleye, Olarewaju, & Fajuyagbe, 2019). The proxies for CG were board size, activism, and committee activism, while the indicators of company performance were ROA and firm growth rate. The data was analyzed using static panel estimate techniques, and the results suggest that CG has a large negative impact on return on asset, but has no effect on the growth rate of multinational enterprises in Nigeria.

In addition, the correlation between CG and the performance of 207 non-financial services firms listed on the Pakistan Stock Exchange from 2003 to 2014 was investigated (Hussain, Ahmad, & Hassan, 2019). Board independence, board meetings, CEO duality, concentrated ownership, institutional ownership, managerial ownership, big 5 ownership, audit quality, and audit committee composition were used as proxies for CG, while board independence, board meetings, CEO duality, concentrated ownership, institutional ownership, managerial ownership, big 5 ownership, audit quality, and audit committee composition were used as measures of performance. The analysis was carried out using GMM and the Arellano-Bond Dynamic Panel-Data estimate approach. Firm performance is influenced by board size, board independence, board meetings, concentrated ownership, institutional ownership, and the audit committee, according to the findings.

As can be seen from the following, strong governance entails limited expropriation of company resources by managers or controlling shareholders, resulting in better resource allocation and performance. Because of lower capital expenses, which is another indicator of business performance, investors and lenders will be more ready to put their money into companies with high CG. Good CG practices attract stakeholders, such as employees, who want to be associated with and work for such businesses because they perceive them to be healthier, more profitable, and more likely to survive than businesses with poor CG.

Providers of funds will be easily drawn and will want to invest in companies that have solid resource management, good performance, and effective governance processes; this will likely lead to lower capital costs, which will boost the company's performance even more (Farhan, Obaid, and Azlan, 2017). The research also found that some existing studies imply a positive and significant relationship between CG and financial performance, while others suggest a positive but negligible relationship, and still others suggest no meaningful relationship between CG and financial performance. As a result, existing literature yields varied and inconclusive results, necessitating greater empirical investigation in this area. The governance gap is substantially related to firm value, according to the findings. There are few research on corporate governance and its impact on financial performance in non-financial listed companies in the UAE. As a result, the purpose of this research is to fill a vacuum in the literature by addressing this critical relationship.

## 2.4. Theoretical Framework

The agency hypothesis is shown to be applicable when looking at the impact of CG on financial performance of listed businesses in the UAE Exchange market. The relationship between the principal and the agent, such as shareholders and firm executives or managers, is referred to as agency theory. Managers are assumed to be self-interested and risk averse under this approach. When managers do not own 100 percent of the company's wealth, they may operate to maximize their own personal wealth rather than the wealth of the shareholders. Furthermore, CSR is an indication of an agency problem or a conflict of interest between management and shareholders (Friedman, & Allen, 1970). The rationale for how a board oversees management on behalf of shareholders is based on agency theory, which has dominated CG research (Davis, Schoorman, & Donaldson, 1997). The separation of ownership and control causes managers' interests to be misaligned with those of shareholders. According to agency theory, one of the key functions of managers is to align the interests of corporations with the interests of shareholders, and the agency relationship is defined as one party, the principle, delegating work to another party, the agent.

The owners are the principal, while the directors are the agent, in the context of a corporation (Davis, Schoorman, & Donaldson, 1997). When it comes to companies and corporate governance, agency theory sees CG mechanisms, particularly the board of directors, as an important monitoring instrument to ensure that any problems caused by the principal-agent relationship are minimized. Furthermore, according to agency theory, principals (shareholders) and agents (managers and other company insiders) have opposing interests, risk tolerances, capacities, and information. Wherever possible, opportunistic management motivated by self-interest and deception will act against outside investors (Davis, Schoorman, & Donaldson, 1997). Shareholders can use a variety of CG mechanisms to challenge this assumption, including contractual relationships, board monitoring systems, and incentives (Shleifer, & Vishny, 1997). These governance methods are intended to ensure that agent-principal interests are aligned, that shareholder interests are protected, and that agency expenses are minimized (Davis, Schoorman, & Donaldson, 1997; Kabir & Thai, 2017). Furthermore, boards exert control by preventing managers from acting opportunistically in order to further their own personal interests. As a result, agency theory provides a foundation for corporate governance through various internal and external methods in order to control the agency problem and attain a desirable level of performance and trustworthy financial reporting (Roberts, McNulty, & Stiles, 2005).

According to agency theory, a larger board size translates to more effective management oversight by diminishing the CEO's dominance on the board, resulting in higher business performance (Singh & Harianto, 1989; Aras, Aybars, & Kutlu, 2010). The board of directors, according to agency theory, controls and monitors management to prevent them from taking actions that benefit them rather than the shareholders. Larger boards can be more effective since the monitoring supervisors' workload can be spread out over a larger number of people. On the other side, with a larger board, agency difficulties might grow more serious, making it easier for the CEO to influence and dominate the board (Cheng, 2008). According to this hypothesis, a larger board might cause coordination and communication problems, allowing profit-driven managers to gain control (Walls & Hoffman, 2013).

When it comes to board independence, agency theory recommends for the use of independent directors since they can better oversee management. Independent directors, as opposed to inside directors who may have a conflict of interest, can ensure that the company's management are operating in the best interests of the company. According to the agency hypothesis, having non-executive directors on the board is critical for ensuring that managers behave in the best interests of shareholders. The usual expectation is that nonexecutive directors will be able to oversee executive directors since they are independent and have the expertise to do so, and that their knowledge and experience in monitoring services would improve business performance (Fama & Jensen, 1983). Agency theory is primarily

concerned with the monitoring function of directors when it comes to board gender diversity. A balanced board will have representation from a variety of groups, ensuring that no single person or group of individuals can dominate the board's decision-making (Erhardt & Werbel, 2003).

Krishnan et al. (2011) considered that the financial expert within the AC should have sufficient expertise to oversee the financial reporting because financial reporting is a process that involves a comprehensive grasp of the accounting difficulties within the organization (Chan et al., 2011). The financial competence of the ACs improves the quality of the financial reports that are prepared (Carcello et al., 2011). Ghafran and O'Sullivan (2013) came to the same result in their evaluation of the importance of the ACs, finding that ACs with more accounting/financial competence have a beneficial impact on financial statement quality. At least one financial specialist is required by the MCGC for the AC members. According to previous studies, such as Chan et al. (2011), the financial expert is required because the AC's primary responsibilities include finance and auditing. While Chan et al. (2011) did not find a direct effect of the financial expert on firm value, they did justify their findings by claiming that the firm value is influenced by the AC's compliance with all of the CG code standards. AC members with financial experience, according to Xie et al. (2003), are more able to detect earnings managements.

The AC should meet frequently and allocate sufficient time to complete the allocated tasks; otherwise, the financial report will be of poor quality. According to Rickling (2014), AC members who do not meet frequently (busy members) have a negative impact on their capacity to oversee financial reports. Meeting more regularly would allow the AC to provide higher-quality financial reports in a shorter amount of time than a less-frequently meeting AC (Ionescu, 2014). When researchers looked at the relationship between the number of meetings held by the AC and the likelihood of earnings management, Xie et al. (2003) discovered that the AC with the most meetings had a negative relationship with earnings management. On the same topic, Abbott et al. (2000) discovered that ACs that meet at least twice a year have a lower likelihood of profits management. According to Article 9 of the MCGC for 2009, the AC should meet at least four times each year (once every quarter). In other words, the research examines the impact of incentives on business performance, keeping in mind that the agency theory posits that performance-based incentives will improve firm performance (Farhan, Obaid, and Azlan, 2017).

### 3. Methods

The study also incorporates documentary data, which was generated from the annual reports and accounts of Fifty Five (55) sampled listed public businesses in the UAE Exchange from Abu Dhabi Emirate and Dubai, and covers the period 2016-2020. A purposive sampling strategy is used to determine the sample size. This study takes into account two types of variables: dependent and independent variables. The financial performance, as measured by ROA, was the study's dependent variable. The return on assets (ROA) was calculated as the ratio of earnings after taxes to total assets (Erhardt & Werbel, 2003). The independent variable, CG (board structure), was proxied by board size, board independence, and board meeting. The number of directors on the board was used to determine the size of the board (Ntim & Soobaroyen, 2013). The number of outside or non-executive directors was divided by the total number of directors to determine board independence (Kabir & Thai, 2017). The number of female directors on a board was divided by the total number of directors (Ntim & Soobaroyen, 2013; Kabir & Soobaroyen, 2013; Kabir & Thai, 2017). For the analysis, descriptive statistics, correlation, and multiple regressions were used. The nature of the relationship between CG and financial performance was determined using the Pearson correlation technique. This demonstrates how strong the relationship between the independent and dependent variables is. Multiple regressions were used to examine the impact of the explanatory variables (board size, board independence, AC features, and company size) on the dependent variable (ROA).

The relevance of multiple regressions in earlier similar studies, as shown in the literature review, influenced the choice of this technique. However, because panel data analysis was used in this study, the pooled OLS regression approach is prone to heterogeneity bias, hence fixed and random effect regressions were also performed. In addition, the F-test was utilized to determine whether fixed effect or pooled OLS regression should be used. The following is the model based on the study's variables:

$$ROA = \beta_0 + \beta_1(BS) + \beta_2(BI) + \beta_3(AC\ IND) + \beta_4(AC\ INC) + \beta_5(AC\ MEE) \\ + \beta_6(FIN\ EXP) + \beta_7(Size) + \beta_8(LEVERAGE)$$

**Table 1 Measurement of variables**

Indicator	Description	Measurement	Reference
ROA	Return on assets	Net earnings divided by the total assets	Mak and Kusnadi, 2005
BS	Board size	Total number of directors on the board	Essen et al., 2013
BI	Board independence	Percent of the independent directors in the board	(O'Connell and Cramer, 2010; Guo and KGA, 2012)
AC INDEPENDENCY	The independent members	The independent members divided by all the AC members	Sharma and Kuang, 2014
AC INCENTIVES	Average fees	The average fees per member that have been received by the AC members during the year	Chan et al., 2013
AC MEETINGS	Number of meetings	Number of meetings held by the committee during the year	Rickling, 2014
FINANCIAL EXPERT	Committee qualification	The proportion of the members within the committee with financial experience or qualifications	Yin et al., 2012; Chan et al., 2013
Firm Size	Size of the company	The natural logarithm of the total assets	Essen et al., 2013
Leverage	The total debt to total assets	Dividing total debt by total assets	(Cho & Park, 2015; Zhou, Pan, & Wang, 2015)

## 4. Results and Discussion

### 4.1. Descriptive Statistics

Table 2 shows the descriptive statistics, which include measures of central tendency such as mean and measures of dispersion (distribution spread) such as standard deviation, minimum, and maximum of the variables. The ROA has a mean of 3.4326 and a standard deviation of 9.7318.

**Table 2 Descriptive Statistics**

Variable	Min	Max	Mean	Std
ROA	-68.423	40.856	3.4326	9.7318
BS	4.000	20.000	9.1244	3.0463
BI	33.33	100.00	70.3641	20.0233
AC INDEPENDENCY	19.00	105.00	90.4322	17.2312
AC INCENTIVES	0.000	5,342.00	3,662.121	7455.7133
AC MEETINGS	0.000	15.000	5.0125	2.0804
FINANCIAL EXPERT	0.000	105.00	38.4322	23.8124
Firm Size	5.123	9.123	7.2312	0.6602
Leverage	0.512	93.0221	46.1232	20.4186

The MCGC does not specify the number of board members, but on average, corporations have nine members on their boards; the majority of them are independent, as seen by the average board independence of (70.3641± 20.0233). According to the MCGC, the AC shall include at least three members, at least one of whom should have financial experience or qualifications. Table 2 shows that the financial specialists' ratio in the ACs has a mean and standard



deviation of  $38.4322 \pm 23.8124$  percent, which is slightly higher than the third. This means that the enterprises followed the MCGC's financial expert ratio guidelines. According to the MCGC, the ACs should meet once every three months, with an average and standard deviation of  $(5.0125 \pm 2.0804)$ , though there may be busy committees with more meetings. Although the average and standard deviation of the rewards provided to AC members per meeting is AED  $(3,626.121 \pm 7455.713)$ , the standard deviation and maximum payout of incentives show that certain firms pay substantially more. The AC independence mean and standard deviation are both high  $(90.4322 \pm 17.2312\%)$ , which could be attributable to the MCGC's unambiguous assertion that the majority of members should be independent. In the United Arab Emirates, the average debt of businesses is relatively high.

#### 4.2. Testing the Multi-collinearity

To test for the multi-collinearity and the association between the independent variables, the variance inflation factor (VIF) and Tolerance values were calculated for each variable Table 3

**Table 3 Multi-collinearity results**

Variable	Tolerance	VIF
BS	0.723	1.612
BI	0.756	1.489
AC INDEPENDENCY	0.815	1.387
AC INCENTIVES	0.825	1.301
AC MEETINGS	0.865	1.286
FINANCIAL EXPERT	0.879	1.121
Firm Size	0.712	1.634
Leverage	0.889	1.201

The results show that all of the independent variables have low Variance Inflation Factors (VIF) values, indicating that multi-collinearity is not an issue (Liu et al., 2003; Chan et al., 2013). The similar conclusion can be drawn about tolerance values that are not close to zero, implying that there is no multi-collinearity.

#### 4.3 Regression Analysis and Result

The regression results for the created model in this investigation are shown in Table 4. The dependent variable in this model is ROA, and we can infer that the model is significant ( $F= 4.122$ ,  $p\text{-value} = 0.001$ ), with an adjusted  $R^2$  of 0.135. The study variables, it may be argued, have an impact on the firm's value as evaluated by ROA. Table 5 shows the regression coefficients for the ROA model, which reveal that Board independence ratio has a negative impact on ROA, which is consistent with prior research by Judge et al. (2003) and Bhagat and Bolton (2008). Bhagat and Bolton (2008) found that board independence is connected with future business performance in a negative way. It argues that having a large number of independent directors reduces the board's motive to serve the company; instead, the board director is more concerned with his own incentives than with the company's performance (Chugh et al., 2011). In certain circumstances, the board of directors' credentials are unrelated to the firms' activity, and most of the time, the same board member serves on many boards. Furthermore, board members in the UAE are known for their good reputation and relationships in the business sector, which may decrease the amount of time they require to complete their tasks.

The instance of the United Arab Emirates has brought attention to the issue of weak financial markets, as it was discovered during the data collection stage that stock trading transactions are limited. All of the aforementioned factors could be contributing to the board's independence having a detrimental impact on the firm's ROA in the UAE. Based on the regression results; hence the AC features have no statistically significant effect on the ROA. According to the regression results, board and AC independence would have a negative impact on the firm's performance, which might be owing to the relationship between the two variables. The board directors choose the members of the AC, hence the two factors are linked.

The number of financial experts and the number of AC meetings have little bearing on the firm's performance. That can be explained by remembering that the establishment of the AC is required by the UAE CG law, hence the AC must meet four times a year, regardless of the quality or realism of the sessions. As a result, mandated meetings are held to avoid legal penalties or to improve their image value rather than to maintain quality. Furthermore, the members

of the AC in the majority of the previously analyzed sample organizations are well-known directors who are busy on many other boards, in addition to a lack of expertise and auditing abilities required to carry out the given tasks. As a result, the study concluded that mandating the formation of an AC and establishing the frequency of AC meetings does not improve the firm's performance.

**Table 4 Model summary**

Variable	R	R <sup>2</sup>	Adj R <sup>2</sup>	F-stat	Sig.	DW
ROA	0.432	0.187	0.135	4.122	0.001	

**Table 5 Regression Coefficients**

Variable	$\beta$	Standardized B	T-Stat	Sig.
Constant	-2.113		-0.458	0.576
Board Size (BS)	0.276	0.112	1.289	0.210
Board Independence (BI)	-0.0501	-0.151	-1.885	0.049
AC INDEPENDENCY	0.012	0.034	0.421	0.699
AC INCENTIVES	0.003	0.010	0.115	0.865
AC MEETINGS	-0.420	-0.113	-1.821	0.789
FINANCIAL EXPERT	-0.011	-0.115	-1.620	0.103
Firm Size	1.521	0.168	2.032	0.039
Leverage	-0.065	-0.187	-3.561	0.001

## 6. Conclusion

The impact of the CG mechanisms on the firm's performance was explored in this study. The CG is a new issue in the UAE. According to the research, revamping the CG in the UAE improves the firm's performance. The study looked into the impact of board size, independence, and AC characteristics on the firm's ROA in particular. The following AC features were looked into: AC independence, meeting incentives, and financial specialists within the AC. The study's aims were assessed using data from publicly traded companies in the UAE financial market, in both Abu Dhabi and Dubai, from 2016 to 2020. Prior governance research has found that, contrary to popular belief, board independence improves a company's performance.

According to this study, independent directors in the United Arab Emirates are not driven to improve the firm's performance. During the data gathering stage, it was discovered that the directors' names appear in multiple firms at the same time, which, combined with the financial markets' weakness, limits the shareholders' true monitoring role of the directors' activities in the firms. The board's independence could have a negative impact on the firm's performance, which the busy directors could misinterpret. The study goes above and beyond the literature by looking at the impact of AC features on company performance. The study discovered that AC's independence had a detrimental impact on the firm's performance, which might be seen as a logical consequence of the board's independence. The AC members are chosen from the boards (they are not outsiders) in order to forecast the relationship between board independence and AC independence. The number of financial experts and the number of AC meetings have little bearing on the firm's performance. The above results could be attributable to a lack of expertise and auditing abilities among the AC, which is required to complete the given tasks, based on the nature and backgrounds of the board members, as well as the recent adoption of the AC requirements.

This issue raises the question of whether mandating the AC formation and establishing the frequency of AC meetings is feasible when it does not translate into improving the firm's performance in the UAE. Furthermore, the study discovered that AC incentives have a negative impact on the firm's performance. In some cases, the AC has received no compensation for their meetings, while in others, the compensation has been substantial. The aforementioned data show that governance in the UAE is not just about enforcing legislation; it also requires a greater attention on the actual execution of such policies. The current study found a positive relationship between firm size and AC meetings and incentives, implying that larger companies are more conscious of the value of the AC and their functions. The

study's findings have some practical consequences for regulators. To begin, it is important to emphasize that all UAE enterprises have complied with the MCGC. However, effort and training are still required for the enterprises to gain the benefits of their adoption. Regulators should place a greater emphasis on the selected AC members based on their financial knowledge. Second, due to the lack of true independence among most board members, more clarification of board independence criteria should be explored in future laws.

The majority of directors have been chosen based on their relationships and positions, while their ability to defend the shareholders' wealth has been overlooked. Finally, the data above point to a number of promising areas for future investigation. One of them is to look into the impact of AC member tenure on the firm's performance, which could help to improve auditing methods by increasing experience and expertise. It's also fascinating to see how the busy directors affect the firm's performance and to dig deeper into the realities of the AC meetings. The true value added by forming the AC should be analyzed, especially when maximizing the firm's worth is one of the key objectives.

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