Developing Country Studies
ISSN 2224-607X (Paper) ISSN 2225-0565 (Online)
Vol.6, No.8, 2016

Effects of Board & Ownership Structure on Firm Financial Performance: An Economic Value Added Perspective

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Abstract
The main objective of the study was to determine and evaluate the impact of corporate governance on firm financial performance, measured by using economic value added method. The study applied Economic value added approach to examine the effects of board and ownership structure on the performance of firms listed on the PSE over the period 2009 to 2014.The sample includes 600 observations from 100 textile firms.EVA is used to measures firm performance. The OLS regression results show a positive relationship between proportion of non-executive directors and firm performance, suggesting the powerful and influential role non- executive director's play as a corporate governance mechanism. The board size and board meeting is positively and significant correlated to the firm performance. In terms of ownership structure, family ownership is positively but insignificantly correlated with firm performance. In contrast, a negative relationship is observed between government ownership and firm performance, implying worse firm performance when government ownership exists. Institutional ownership is also negatively correlated with firm performance.
Keywords: Ownership Structure, Board Composition, Corporate Governance, EVA.

1. Introduction

Every corporation, wants to grow has several stakeholders such as shareholders, suppliers, Investors, customers and local community. For survival and growth, organizations have depends on to build the sound relations with all stakeholders .Corporate governance play a vital role in building sound associations. Corporate governance refers to the rules, process and practices by which the companies are governed and controlled (Kumar, 2003).

Ownership structure is a mechanism of corporate governance. This study examines the effect of three types of ownership on firm performance that is the, institutional, family and government ownership. Ownership structure refers to the proportion of stock possess by the stockholder with regard to votes and stock as well as the identity of stockholders. These Ownership structure are important in corporate governance they determine the remunerations of managers and they manage the economic efficiency of the firms (Jensen & Meckling, 1976).

Institutional ownership is defined by Chung &Zhang (2011) the proportion of firm stock is hold by institutional investors. Institutional owners are considered to be more skilled in investing due to the assumed technical nature of operations and easy access to firm and management because of that large size of institutional investors firm. They can guide/direct the board and have diversified investment portfolio so they face less risk than non- institutional owners (Khanchel, 2007).

The family owned business are correlated with the common vision of the business, long term objective, and a commitment to grow the family assets instead of harvesting those assets (Miller &LeBeton –Miller, 2005) .Families generally agreeable to subordinate their owns objectives and goals are also probably to act less with less selfish spirit and self promotion (Sciascia & Mazzola, 2008).Government ownership in the companies is reducing the agency problems. Government ownership can align the interest of both parties (e.g. owners and managers) and also provide the symmetry information to the both parties regarding the firm performance. (Jenson and Mechkling, 1976).Usually, government is the ability easily obtaining the information from all firms.

Board is another mechanism of corporate governance. Board also plays an important role for smooth working of an organization. This study examines the effect of three dimensions of board structure on firm performance that is the, board size, board composition and board meeting. Board size refers to the number of directors in the board for specific financial year. There are not specific rule that the number of directors in the enterprise can have. Board size cannot be fixed for the countries because countries are not same in economic, legal, company and social environment (Dalton et al., 1998).Lipton & Lorch (1992); Hermalin &Weisbach (2003) and Jenson (1993) suggest that board should have a maximum of seven or eight members to function effectively.

Board composition differ from country to country, the board composition includes executive and non-executives directors. The executives directors are the part of the enterprise thus are executives directors is a person that work as a manager of the company (Clifford &Evans, 1997).The non-executives directors are directors who have no personnel connections and business dealing with the firm either directly or indirectly (Agrawal and Knoeber, 1996).The presence of non- executive directors on board generally improves the board effectiveness (Adams and Mehran, 2003).

Board meeting board of directors held usually in specific intervals to discuss the problems and to make decisions regarding direction of company (Lawler & Finegold, 2006).The frequency of board meeting is probably to increase the firm performance and perform their work according to their interest of shareholders (Lipton & Lorch, 1992).

The objective of the proposed study is to evaluate and determine the impact of board and ownership structure on financial performance and is expected to contribute significantly in the ownership structure and firm performance literature in Pakistan with specific implications for practitioners, policy makers and researchers. The rest of this paper is organized as follows: the Section 2 presents previously conducted studies in the same area; Section 3 presents the theoretical framework. Section 4 discusses the methodology and definitions of variables for the analysis. Section 5 presents empirical results. Section 6 discusses the recommendation of this study and the conclusions drawn.

2. Literature Review

The globalization of business operation and financial crises that has prominent corporate governance in the research.Most countries has made the remarkable efforts for transparency and disclosure of information in business. Corporate governess addressed to the process and system through which the policies and key issues of the companies are directed and controlled (Fama & Jenson, 1983).Ownership structure is a significant mechanism of corporate governance and its importance cannot be overlooked in boosting up the firm performance (Shleifer and Vishny, 1997).

Dyer (2006) suggests that family firms owned the specific resources as well as reduce the agency cost. Family owners invests for longer time horizons, more efficiently manage the business oversee the activities and work of manager better (Stein, 1998 and James, 1999). Moreover, Villalonga and Amit (2006) examined that family owned firms in Italian 500 companies from 1994 to 2000 performance these companies increase as well as revenue growth over time. In contrast, Filatotchev et.al (2011) observed that using the sample of 228 companies listed in Taiwan stock exchange.

Douma et al. (2006) examined the effect of institutional ownership and firm performance. They taking the 1005 companies listed on Bombay stock exchange over 1999-2000 using the OLS regression techniques and find out the positive association between institutional investors and firm performance. Mashayekhi and Bazazb (2008) evaluate the relationship between institutional investors and firm value. They employed a sample of all companies listed on Tehran stock Exchange through 2005 to 2006.They were using Multiple regression techniques and show that negative relationship between institutional ownership and firm value. Xu and Wang (1999) assessed the impact of state ownership on firm performance. He took the sample of 6993 Chinese listed companies from 2008 to 2014 and used the OLS regression techniques that show the negative impact of state ownership on firm performance by the reason of the aim government owners is the society welfare instead of profit maximization

Uadiale (2007) examined that the positive association between firm value and board size were using OLS regression model and taking the sample 30 companies listed on Nigerian stock exchange. In contrast, Yokishawa& Paun (2004) also reported that negative association between board size and firm performance (in terms of market-to-book ratio and ROA) for Japanese corporation. The study conducted by Husein (2010) and Awan (2012) examined that positive correlation between outside directors and firm value because that asymmetry information is prevail in the firm. Al- Matari (2012) determine that board independence is negative related to the firm performance. They were taking the sample of 136 Kuwait firms for the period 2009 and used the multiple regression analysis.

Dar et al. (2011) find out frequency of meeting is positively related to firm performance.

Carocello et al. 2002 observed that using the sample of 307 US listed companies from 1990 to 1994 found that the negative association between firm performance and board meeting. In the context of Pakistan, Safdar Husain Tahir and Hazoor Muhammad Sabir (2014) find out the relationship between family ownership structure and firm performance. This study using a sample size of 228 companies listed on PSE collected the data from 2002 to 2013.using the Generalized Method of Moment and find out the positive relationship between family ownership and firm performance. Moreover, Nadeem Ahmed Sheikh and Shoaib khan (2011) revealed that positive impacts of board size on firm performance using the data of non-financial companies listed on PSE Pakistan from 2004 to 2008.Furthermore, Atiqa Rehman and Syed Zulifqar (2013) analyzed that significant positive association between board independent and firm performance used the sample of eighty companies listed on PSE over 2005 to 2009.

The most considerably problem of corporate finance is how to accurately measure the firm performance. Marshall (1890) called this performance measure is the' residual income '. It is defined as a after -tax net operating income minus capital charge. According to Anderson, Anne et al. (2005) companies earnings more than cost of capital, in order to create the value for shareholder. Stern Stewart (1990) popularized the concept of EVA and suggests that measure is almost 50 % is better than accounting performance measure is explaining the variability in shareholder wealth.EVA is the important measure because other traditional measure only explains the specific situation or market. For example earning per share only explains the capital market but not explain the capital

budgeting .EVA explains the capital budgeting and net assets at the same time. There are not any accounting performance measures which explain the changes in shareholder wealth (Chen & Dodd, 1997).

EVA is the vale created by management for the shareholder. Today management is to find the means to create the value for shareholder .Eva is the best measure to evaluate the performance of firm that is calculated as follows:

EVA=NOPAT-(invested capital*WACC)

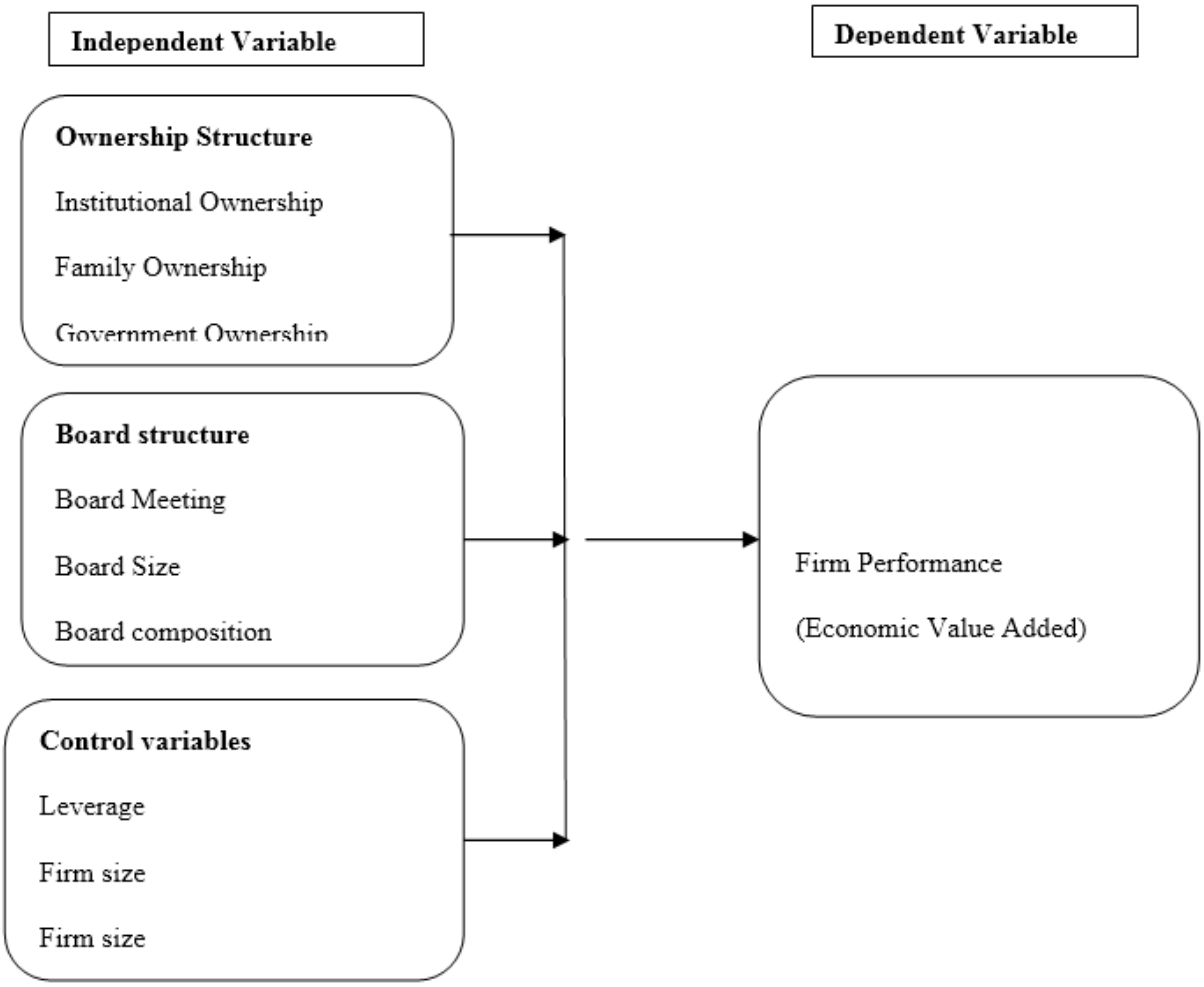
NOPAT: is the income derived from operations after taxes. It is the total profits that are available to provide cash return to those who provide the capital to the company.

Invested capital: the amount of capital is invested in business. It is calculated that the sum of all interest bearing debt and equity or the sum all invested assets in firm and non- interest bearing current liabilities (total assets minus current liabilities).

WACC: is the Cost of debt and equity.

3. Conceptual Framework

After reviewing the literature the theoretical framework of the study is developed that represent the impact of board & ownership structure on financial performance of business. It also represents the significant impact of institutional, family and government ownership, board size, board composition and board meeting on performance of textile industry of Pakistan. The independent variable of the study is board & ownership structure. The dependent variable of the study is financial performance whose one indicator, EVA is used to measure it. The model of the study is presented as follows:



Supporting studies :(Lin & Wu, 2010; Haniffa & Hudaib, 2005; Al-Hussain & Johnson, 2009; kang & kim, 2012; Coleman, 2007; Villalonga &Amit, 2006; Javed & Saeed, 2013).

4. METHODOLOGY

Data Description:

In order to investigate the impact of board & ownership structure on financial performance, present study selected textile sector firms listed at Pakistan Stock Exchange during 2009-2014. The textile sector contributes more than

60% of total export and largest manufacturing sector of Pakistan economy. There are 100 firms selected and there are 600 observations. Panel Data for this study has been collected from Annual reports of Pakistan Stock Exchange (PSE), Published financial statements of companies.

Variables:

Definitions of variables are reported in Table 1. Notably, definitions are extracted from literature relevant to corporate governance so that results of this study can be compared with prior empirical studies.

Table.1: Definition of Variables

Variables	Proxy	Definitions
Dependent Variable		
Economic value added	EVA $_{it}$	NOPAT(Invested capital*WACC)
Independent Variables		
Institutional ownership	INST.OWN $_{it}$	The percentage of shares held by institutional investors.
Family ownership	FAM.OWN $_{it}$	Proportion of shares owned by family members.
.Government ownership	GOVT. OWN $_{it}$	Proportion of shares owned by government.
Board meeting	B.METING $_{it}$	Numbers of Board Meeting held in financial year.
Board size	β_6 B.SIZE $_{it}$	Total number of directors on the board
Board composition	B.COMPOSITION $_{it}$	Proportion of Independent Directors on the Board.
Control variables		
Firm size	F.SIZE $_{it}$	Natural log of total assets.
Firm age	F.AGE $_{it}$	Number of years since a firm is incorporated
Leverage	LVRG $_{it}$	Total debt/Total assets

Fixed Effect Regression Model

$$EVA_{it} = \beta_{1i} + \beta_2\ INST.OWN_{it} + \beta_3\ FAM.OWN_{it} + \beta_4 GOVT.OWN_{it} + \beta_5\ B.METING_{it} + \beta_6\ B.SIZE_{it} + \beta_7\ B.COMPOSITION_{it} + \beta_8 F.SIZE_{it} + \beta_9\ F.AGE_{it} + \beta_{10} LVRG_{it} + \mu_{it}$$

Random Effect Regression Model

$$EVA_{it} = \beta_{1i} + \beta_2\ INST.OWN_{it} + \beta_3\ FAM.OWN_{it} + \beta_4 GOVT.OWN_{it} + \beta_5\ B.METING_{it} + \beta_6\ B.SIZE_{it} + \beta_7\ B.COMPOSITION_{it} + \beta_8 F.SIZE_{it} + \beta_9\ F.AGE_{it} + \beta_{10} LVRG_{it} + \omega_{it}$$

5. RESULTS AND DISCUSSION

This section presents the empirical findings or results of the relationship that exists among variables selected in current research. First of all it presents the descriptive or summary statistics, which shows the properties of the data. This section also presents the penal data models such as, fixed effect model and random effect model, as well as theoretical discussion on results of these models. In addition Hausman specification test is also shown to present which model batter explains the required relationship. Finally the results of each hypothesis are also discussed in details.

Table2. Descriptive statistics

Variables	EVA	FAM.OWN	GVT.OWN	INST.OWN	LVRG	METING	PNED	F.AGE	BS	F.SIZE
Mean	7.8888	41.6401	4.8887	4.3114	42.4828	4.9340	58.888	37.807	7.445	20.721
Median	7.0247	42.1950	2.1900	1.7700	0.6976	5.0000	57.140	41.000	7.000	21.125
Minimum	2.085	99.910	24.120	45.000	821.76	9.000	100.000	68.000	10.00	24.310
Maximum	-1.254	0.0500	0.010	0.000	0.006	4.000	22.2200	15.000	5.000	15.290
Std.Dev.	9.332	25.574	5.8434	7.527	169.32	1.0751	16.4584	14.643	0.708	2.1173

Descriptive statistics is presented in Table 2. This table shows different statistical facts about data such as mean, medians, standers deviation, skewness and Kurtosis of all dependent, independent and control variables As shown in the table; average firm performance is 7.888 with a range from -1.254 to 2.085, suggesting that the majority of firms have better performed. Board size in PSE listed firm's ranges from 5.00 to 10.00 directors with 7.445 being the average, suggesting that most Pakistani listed firms have sufficient directors. Concerning with the proportion of non-executive director the average value is 58.888 with a range from 22.220 to 100.00, suggesting inclusion of non-executive was also supporting in boosting firm value. Among the different groups of ownership, family ownership records the average value is 41.640 with a range from 99.910 to 0.500.Government ownership records the mean value is 4.8887 ranging from 0.010 to 24.120 while standard deviation is 5.843.Moreover, the mean of institutional ownership is found to be 4.311 ranging from 0.000 to 45.000 while standard deviation is 7.5227.The average of firm meeting is 4.934 ranging from a minimum of 4 meetings to a maximum of 9 meetings. The average firm age is 37.807 while the maximum and minimum are 68.000 and 15.000 respectively. In addition to that, the mean of the firm size is 20.721 while the maximum and minimum are 24.310 and 15.290 respectively with standard deviation of 2.117. Similarly, the mean of the leverage is 42.482 while the maximum and minimum are 821.76 and 0.006 respectively with standard deviation of 169.32.

Table.3 Correlation Matrix

Variables	1	2	3	4	5	6	7	8	9	10
AGE	1									
BS	0.25	1								
EVA	0.84	0.65	1							
FAMOWN	--0.05	0.34	0.86	1						
GOVTOWN	-0.11	-0.14	-0.91	-0.2	1					
INSTOWN	0.14	-0.22	0.75	-0.12	-0.13	1				
LEVRAGE	0.32	-0.13	0.55	0.55	-0.11	0.12	1			
MEETING	-0.12	-0.23	0.65	-0.45	0.15	0.12	-0.1	1		
PNED	-0.04	0.19	0.74	-0.44	-0.34	0.1	0.19	-0.13	1	
SIZE	-0.14	0.13	0.77	0.33	0.2	-0.06	-0.4	-0.32	0.2	1

Correlations of variables are presented in Table 3 which indicates that firm age is significant and positively correlated with board size. Similarly, EVA, Inst ownership and leverage is also positively correlated to the firm. In contrast, firm age is negative correlated with family and Govt. ownership, board meeting, proportion of non-executive director and firm size. Moreover, board size is positive correlated with family ownership, EVA, proportion of non-executive director, and firm size. Although, board size is negative correlated with Govt. and Inst ownership, leverage and meeting. Furthermore, the relationship of EVA is negative with Govt. ownership which is (-0.91). However, EVA is positively related with family and Inst ownership, board meeting, leverage, firm size and proportion of non-executive director. So, this table identifies the relationship of all variables with each other.

Table.4 Regression Results

Variable	Coefficient	Std. Error	P-value
C	7.371780	4.817921	0.1279
AGE	0.060662	0.223980	0.0568
BS	0.132603	0.591987	0.0030
FAMOWN	0.143447	0.352879	0.6849
GOVTOWN	0.066754	0.122785	0.0384
INSTOWN	0.184432	0.222146	0.2076
LEVERAGE	0.315740	1.455002	0.6497
MEETING	0.060458	0.368912	0.0400
SIZE	1.154693	2.128877	0.0183
PNED	1.781885	7.225585	0.0455
R-squared	0.551811		
Adjusted R-squared	00.32197		
F-statistic	1.044273		
Prob(F-statistic)	0.006937		

In table 4 the OLS regression results indicate that there is significant association between EVA and board size. The t- value and p-value are respectively significant and according to the thumb rule, i.e. $t > 2$ and $p < 0.05$. Board size which is independent variable shows a positive significant impact on EVA. The second dimension of corporate board composition i.e., non-executive director is also significant to the firm performance as measured by EVA. Meeting of the board shows a positive significant effect on EVA. The fourth independent variable which is the family ownership signifies an insignificant impact on economic value added**.** Government (negative significant -2.54) and institutional ownership which are also independent variables shows insignificant effect on firm performance as measured by EVA. Leverage of the firm which is controlled variable shows an insignificant impact on firm value. Size of the firm which is controlled variable signifies the highly significant impact of EVA. Firm age which is also controlled variable shows a significant impact on firm performance.

Goodness of fit of model is checked by the coefficient of determination R2. Coefficient of determination provides the extent to which change in dependent variables is explained by the change in independent variables. Overall the R- squared of the model shows that (0.551811) percent variation in EVA is due to the independent and controlled variable incorporated in the econometric equation.

Hausman Test
Correlated Random Effects - Hausman Test

Test cross-section random effects

Test Summary	Chi-Sq. Statistic	Chi-Sq. d.f.	Prob.
Cross-section random	793.967199	11	0.0000

After estimating the fixed effect model Hausman specification test has been employed to determine whether random effect or fixed effect is best to explain the relationship between dependent variable and explanatory variable. According to the Hausman specification test , the p value is highly significant therefore the null hypothesis and alternate is accepted therefore, the study employed the fixed effect model to explain the relationship between dependent and independent variable.

Table 5 .Fixed Effect Model Results

Variable	Coefficient	Std. Err	P-value
C	3.28E-05	1.15E-05	0.0051
AGE	1.83E-08	9.40E-08	0.8457
BS	2.87E-06	8.90E-07	0.0016
EVA	1.000000	3.57E-17	0.0000
FAMOWN	1.05E-07	5.36E-08	0.0525
GOVTOWN	-2.62E-07	1.22E-07	0.0336
INSTOWN	-8.11E-08	1.39E-07	0.5610
LEVERAGE	-1.36E-08	4.75E-09	0.0049
MEETING	2.25E-06	4.17E-07	0.0000
PED	4.31E-08	4.61E-08	0.3516
PNED	5.13E-08	4.19E-08	0.2233
SIZE	-3.50E-06	3.32E-07	0.0000

R-squared	1.000000
Adjusted R-squared	1.000000
F-statistic	2.50E+31
Prob(F-statistic)	0.000000

In table 5 the fixed effect models results indicate that there is significant association between EVA and Board size. The p-value is significant and according to the thumb rule, i.e. $p < 0.05$. Board size which is independent variable shows a positive significant impact on EVA. The second dimension of corporate board composition i.e., non-executive director shows an insignificant impact on the firm performance as measured by EVA. Meeting of the board shows a highly significant effect on EVA. The fourth and fifth independent variables which are the family and Government ownership signify a significant impact on economic value added**.** Institutional ownership which is also independent variable shows insignificant effect on firm performance as measured by EVA. Leverage of the firm which is controlled variable shows significant impact on firm value. Size of the firm which is controlled variable signifies the highly significant impact of EVA. Firm age which is also controlled variable shows a highly insignificant impact on firm performance.

Discussion

This study examines the influence of board and ownership structure on firm‘s economic performance in Pakistan. Board size which is independent variable shows a positive significant impact on EVA. This refers us that larger board size gives the corporations more opportunity to grow and to have better control on the resources of the corporation. The result is consistent with previous studies, such as Van den Berghe & Levrau (2004), Adams & Mehran (2005) and Fauzi & Stuart (2012) confirm that large boards provide the greater monitoring The second dimension of corporate board composition i.e., non-executive director is also significant to the firm performance as measured by EVA indicates that non-executive directors can add potential economic value to the corporation in Pakistan. Rashid, Fairuz, and Husein (2010), Awan (2012), and Liang and Li (1999) also found significant positive correlation between proportion of non-executive director and firm performance.

Meeting of the board shows a positive significant effect on EVA which indicates that corporate board

meet more frequently have increased the capacity to effectively advice and monitor management. Our finding is consistent with empirical studies (Mangena &Tauringana, 2008; Natim & Osei, 2011) that suggest a positive association between board meeting and firm performance.

The fourth independent variable which is the family ownership signifies an insignificant impact on economic value added**.** Institutional ownership is negative and insignificant correlated to the firm performance. Our evidence also provides support for the previous studies (Afza and Nazir, 2015; Zeitun, 2007). Suggest that negative correlation may be due to the different types of investors (active vs. passive) with different motives (long term vs. short term) that may assign the different values to the corporation which may results not significant. Government ownership is significant and negatively related to the firm value. This result is consistent such as Tran, Nonneman& Jorissen (2012), Ng et al., (2009) and Lizal (2002), who indicates government ownership, reduces the firm value. Because the governments focus is social benefit rather than profit.

Regarding the control variable used in this study, we find the positive and significant association firm age and firm value. Our findings is consistent with Bernardo (2002) and Chen (2008) who argued that this positive correlation may be due to older firms possession of more expertise and international operations. The Leverage is positively associated to the firm value suggest that borrowers can use debt as signaling device. It brings motivation in managers to make efficient utilization of resources to meet the obligations of debt repayment and interest so that improves its firm performance (Leland & Pyle, 1977). This finding is consistent with O'Connelly et al., 2012 and Khatab et al., 2011, who concluded that there is positive relationship between leverage and firm performance.

In terms of firm size, it is found to exhibit positive and significant association between firm value and size of firm. This indicates that large size of firms is more resourceful and may achieve cost reduction through economies of scale and can increase their firm profits. Chhibber and Majumder (1999), Kuntluru, Muppani, and Khan (2008), Omrana et al. (2008) and Pathirawasam and Wickremasinghe (2012) also found the direct relation between larger firm size and EVA.

Goodness of fit of model is checked by the coefficient of determination R2. Overall the R- squared of the model shows that (0.551811) percent variation in EVA is due to the independent and controlled variable incorporated in the econometric equation.

6. Conclusion and Recommendation

This paper basically examined the relationship between board, ownership structure and the performance of 100 listed firms in the Pakistan Stock Exchange over the period 2009 to 2014.The board structure studied comprise (board size, board composition, board meeting) and ownership structure is represented by (family, government, institutional) are independent variables of this study. Performance is measured in terms of EVA. Findings from this study show that there is a positive association between board size and firm performance .This indicates that larger boards provide the greater monitoring to mitigate the agency problems. The Proportion of non executive directors is positively and significant related to the firm performance. Suggest that non-executive director is more likely to act in shareholder best interest and improve firm performance through better monitoring of management. The board meeting also is significant and positively related to the firm performance. The positive results confirm that the board effectiveness depends on the frequency of its meetings as this can increase the performance of the firm given the fact that the board is provided with more opportunity of monitoring and reviewing the performance of management.

In case of ownership structure, it was found association of insignificant nature exists between family ownership and firm value. This indicates family businesses have strong control on many decision; they are in better position to expropriate wealth away from minority shareholders. Institutional ownership has also insignificant impact on firm financial performance. This indicates the negative and insignificant correlation due to the different types of investors (active versus passive) with different motives (long versus short) may assign the different value to the firm. Government ownership impact the firm performance is inversely, because government firms have the politically objectives carry the more debt than other firms.

Recommendation

In this research we only employed the textile manufacturing firms listed in Pakistan Stock Exchange, so we recommend future research employed the other manufacturing and non-manufacturing companies.

Secondly, future research that tries to investigate the relationship between boards, ownership structure with company performance can also include other control variables to the study such as industry effects, firm risk, other board characteristics, and the capital intensity.

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