Impact of Corporate Governance on Bank's Financial Performance

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Abstract
The objective of this study is to investigate empirically the impact of corporate governance on banks' financial performance in Ethiopia using panel data over the period 2005-2021. Since the data is secondary in nature, the quantitative approach to research was used to measure the impact of corporate governance mechanisms on banks' financial performance which is measured by ROA. As well, the Feasible Generalized Least Square (FGLS) estimation was used. The FGLS is preferred to the pooled OLS, fixed effect, and random effect model based on the joint effect of an entity in the pooled, variation across entities has not random and correlated in the random effect model, and heteroscedasticity and serial correlation problem in the fixed effect model. The overall FGLS regression result reveals that the model is significant at a 1% level. The regression analysis that six explanatory variables have been found significant effect on the financial performance of bank firms in Ethiopia, management efficiency and asset quality had a negative significant impact on bank performance, whereas bank size, liquidity ratio, legal reserve, and loan to deposit ratio were positively and significantly affect bank performance.
Keywords: Commercial Banks, corporate governance, financial performance, panel data, Return on Assets, Ethiopia.

1. INTRODUCTION
1.1. Background of the Study
Ethiopian banking history, in its modern sense, began towards the end of the reign of Emperor Menilek. During that period, the first bank of the country named "Bank of Abyssinia" was established, which was opened by the emperor on February 16, 1906. This bank was fully managed by the National Bank of Egypt. By 1931, after Emperor Haile Selassie came to power, the Bank of Abyssinia was legally replaced by the Bank of Ethiopia. The new bank "Bank of Ethiopia" was a purely Ethiopian institution and the first indigenous bank in Africa, which was officially established on August 29, 1931, with a capital of £750,000. (NBE)

Following the demise of the Dergue regime in 1991 which ruled the country under the rule of the command economy, the EPRDF declared a liberal economic system. Consequently, shortly after the proclamation the first private bank, Awash International Bank was established in 1994, Dashen Bank was established on September 20, 1995; Bank of Abyssinia, Wegagen Bank, Nib International Bank, Cooperative Bank of Oromia, Zemen Bank, and Oromia International Bank following the above-mentioned banks, they started working in succession.

The motive of corporate governance is to assist construct surroundings of trust, transparency, and responsibility vital for fostering long-time period funding, economic stability, and commercial enterprise integrity, thereby assisting more potent boom and greater inclusive societies (Organization for Economic Cooperation and improvement, OECD, 2015).

In Ethiopia, the National Bank is accountable to keep a strong price of charge and exchange, fostering a wholesome economic machine, and mission such different associated activities as are conducive to the fast financial improvement of Ethiopia. Hence, the National Bank of Ethiopia has issued Bank Corporate Governance Directives No SBB/62/2015 to provide a manner to balanced risk-taking and enhancing business prudence, prosperity, and corporate accountability with the ultimate objective of realizing long-term shareholders' value and customers' and other stakeholders' interest.

1.2. Statement of the Problem
According to Onakoya et al. (2012), corporate governance is about building credibility, ensuring transparency and accountability similarly maintaining a good channel of knowledge disclosure that fosters good corporate performance.

Knowing the importance of corporate governance, several studies are conducted in Ethiopia on the connection between corporate governance mechanisms and firms' financial performance; Study conducted by O. Sakilu, B. Kibret (2015), analyzed the determinants of the financial performances of commercial banks in Ethiopia using time series data covering the period of 2008-2013. The study finds that qualified directors on the board has a statistically significant and negative effect on banks' performance. The frequency of board meetings

on the financial performance of the bank is a positive and significant effect on banks' performance (ROA). On the other hand, variables such as board size, female director in the board, and the existence of audit committee in the board did not have a statistically significant effect on bank's performance. Fanta A.B., et al. 2013, examining the corporate governance mechanisms and their impact on performance of commercial banks in Ethiopia. The findings indicated that board size and the existence of an audit committee on the board had a statistically widespread terrible impact on bank performance; while bank size had a statistically significant positive and superb impact on bank performance.

Ferede, Y. (2012), reported that large size board and audit committee negatively influences financial performance; the percentage of female directors does not have a significant effect on financial performance in Ethiopia. Kebede F. (2016), examining the Effect corporate governance in firms' financial performance using ten years data from the year 2005 to 2014 with a sample of nine Ethiopian commercial banks. The findings of the regression results indicated that board size and audit committee negatively influences financial performance.

The results of the studies show the various impacts of the company governance proxies in terms of significance level and direction of relationship to a bank's financial performance. There's also an inclination of the studies to use internal corporate governance variables instead of using mixed corporate governance variables. Therefore, this study intended to extend the number of observations through the utilization of an oversized sample size and long years of information that's not covered by those scholars.

Therefore, this study will boost existing knowledge and minimize the gap by detecting the impact of selected internal and external corporate governance mechanisms on the financial performance of banks in Ethiopia. The study answers the questions below.

1. How does the internal corporate governance impact the bank's board structure and performance including board size, board gender diversity, audit committee size, meeting frequency of board, and management efficiency?
2. How do the external corporate governance impact on the financial performance of the banks by using financial ratios including asset quality, loan to deposit ratio, liquidity position(ratio), legal reserve and bank size measured by return on assets (ROA)?

2. LITERATURE REVIEW
2.1. Definition of Corporate Governance
Corporate governance deals with the ways suppliers of finance to corporations assure themselves of getting a return on their investment (A.Shleifer & RW.Vishny 1997, p. 737).

The term corporate governance essentially refers to the relationships among management, the board of directors, shareholders, and other stakeholders in a company. These relationships offer a framework inside which company goals are set and overall performance is monitored" (Mehran H. 2003, p.1).

A more comprehensive definition of corporate governance is also provided by Rezaee (2009) as "the process affected by a set of legislative, regulatory, legal, market mechanisms, listing standards, best practices, and efforts of all corporate governance participants, including the company's directors, officers, auditors, legal counsel, and financial advisors, which creates a system of checks and balances to create and enhance enduring and sustainable shareholder value, while protecting the interests of other stakeholders".

2.2. Corporate Governance in Africa
Corporate governance has existed for centuries and has taken a stronger foothold in developed economies when compared to emerging economies. However, African economies began to pay particular attention to the ideals of good governance at the beginning of the 1980s. According to Soyibo, et al (2002) cited by Olayiwola, the term good governance was first mentioned in 1989. World Bank report on Sub-Saharan Africa but since the 1990s many donor agencies have sought the pursuit of good governance (Olayiwola, W. K. (2010).

In Africa, the numbers of listed companies are few and most of them are family or small private enterprises and state-owned corporations that are characterized by a weak regulatory and supervisory framework (Okeahalam & Akinboade, 2003).

According to Africa"s corporate governance network (ACGN) research conducted in 13 countries in February 2016, the implementation of corporate governance is at different stages of progress. South Africa is most advanced in this regard followed by Mauritius, Kenya, and Nigeria. Uganda and Zambia have shown good progress while Zimbabwe is regressing (ECA, 2005).

2.3. Corporate Governance in Ethiopia
According to Kefale (2019), Ethiopia has no separate corporate governance regulation, rather corporate governance issues are covered under the company law part of the 1960 Ethiopian commercial code. The Ethiopian business code has now no longer been amended when you consider that 1960 and with the new corporate exercise trend; the corporate governance provisions aren't cutting-edge and modern to reply state-of-

the-art governance problems. Apart from its obsoleteness, company governance problems aren't protected holistically under the commercial code and lots of company problems continue to be unanswered.

Roberston (2009) and Negash (2008) as quoted in Tsegabirhan (2015), since the regime change from a Military Government to a Transitional Government in 1991, Ethiopia has launched a series of economic adjustment and reform programs geared toward building a competitive private sector. This set of reforms has increased the size and role of the private sector. Even though the economy is dominated by smallholder agricultural activities, over the last two decades, the number of corporate forms of business firms has increased due to the liberalization of the economy. This development has increased the awareness and importance of corporate governance and drawn much attention to guarantee the protection of investors" interests and thereby encouraging and boosting investment.

As per the financial directives for Bank Corporate Governance, "Corporate governance" means the process and structure used to direct and manage the business and affairs of a bank towards enhancing business prosperity and corporate accountability with the ultimate objectives of realizing long-term shareholders''' value as well as customer's and other stakeholder's interests (Bank Corporate Governance, 2019).

2.4. Empirical studies

Getahun, K. (2013), investigates corporate governance mechanism on company performance in Ethiopia. The study adopts quantitative method research approach by combining documentary analysis and administrating simple questionnaire. The findings of the study reveals that deposit ratio and availability of audit committee had a positive and significant impact on banks performance.

Fanta A.B., et.al. (2013), studies the corporate governance mechanisms and their impact on performance of commercial banks. The have a look at used based evaluation of documents, and business banks monetary records have been gathered masking a duration 2005 to 2011. The findings indicated that board size and presence of audit committee with inside the board had statistically giant poor impact on financial institution performance; while bank size had statistically giant high-quality impact on financial institution performance.

OB Sakilu, BG Kibret (2015), examine the determinants of the financial performances of commercial banks in Ethiopia using a time series data covering the period of 2008-2013. In their study, financial performance is measured by ROA of the banks. The study finds that the effect of frequency of board meeting on financial performance of bank is positive and significant.

Kebede F. (2015), studied the Effect corporate governance in firms' financial performance using ten years data from the year 2005 to 2014. The study utilizes panel data and fixed effect regression model analysis. The findings of the regression results indicated that board size and audit committee negatively influences financial performance.

3. Research Method
3.1. Research Design
To conform to the objective of this research, the primary aim of this study will be to examine the impact of corporate governance on banks' financial performance in Ethiopia. To achieve this objective the stud used a mixed research approach.

3.2. Population and Sample
The population of the study was all commercial banks operating in Ethiopia. To select sample commercial banks purposive sampling technique was used, that is based on the availability of data for the study period. According to the information that obtained from the National Bank of Ethiopia this study select seven banks that have completed financial statements for the study period out of the total banks operating in Ethiopia. Those commercial banks was selected as a sample i.e. Awash International Bank(AIB), Bank of Abyssinia(BOA), Commercial Bank of Ethiopia (CBE), Dash Bank(DB), Wegagen Bank (WB), Hibret Bank(HB), and Nib International Bank(NIB).

3.3. Source of Data
Regarding sources of data, the study used secondary sources data. The secondary source of data obtained from the National Bank of Ethiopia and the selected sample commercial banks' official websites over 17 years (2005 - 2021).

3.4. Methods of Data Analysis
Due to the combination of cross-sectional data and time-series data, the OLS regression technique is unsuitable for the analysis (Learner 1978). The applicable method of analysis comprises panel data regression techniques. The big advantage of working with panel data is that can be able to control for individual specific, time invariant, unobserved heterogeneity, the presence of which could lead to bias in standard estimators like OLS. To analyze

the collected data Pooled OLS, Fixed and Random Effect as well as feasible generalized least square regression methods was employed.

3.5. Model specification

In this study, panel data was used. Panel keeps the same individuals or objects and measures some quantity about them overtime. Accordingly, to estimate the effect of corporate governance on bank's financial performance in Ethiopia the following equation as adopted from Brooks (2008):

$$Y_{it} = \alpha + \beta_i X_{it} + \varepsilon_{it},$$
$$\text{for } i = 1, 2, \dots n; \quad t = 1, 2, \dots, T;$$

Where:

- Y_{it} represents the dependent variable (ROA) of the bank i for time period t
- X_{it} is vector of good governance (independent) variables of the commercial bank i for time t
- i indexes for the cross-sectional dimension
- t indexes the time series dimension
- ε_{it} is the error term

3.6. Variables and Measurements

In this study, the variables are selected based on theories and previous empirical studies related to corporate governance and firm performance.

In this study, the dependent variable or a proxy for the commercial banks financial performance which measures a firm's financial performance annually. The frequently used profitability measure, Return on assets (ROA) is an indicator of how profitable a company is relative to its total assets. ROA gives an idea of how efficient management is at using its assets to generate earnings and it is calculated as profit after tax divided by total assets.

The independent variables were variables that are used as a determinant of corporate governance of the Ethiopian bank industries in this study. The independent variables of the study are size of board, board gender diversity, audit committee size, frequency of board meeting, management efficiency, asset quality, legal reserve, liquidity ratio, loan to deposit ratio and bank size.

Table 1 Variable Measures

Variable	Expected sign	Measures
Audit committee size (ACS)	-	Number of audit committee
Board size (BSZ)	+	The number of Directors represent the board
Management Efficiency (MEF)	-	Ratio of non-interest expense to net interest income plus non-interest income
Asset Quality (AQ)	+	Ratio of Provision for Loan to Total Loan.
Bank Size (BKS)	+	Log function of total asset
Legal reserve (LER)	-	Ratio of total reserve to total asset
Liquidity ratio (LIQ)	-	Ratio of liquidity to total deposit
Loan to deposit (LTD)	+	ratio between the bank's total loans and total deposits

4. RESULTS AND DISCUSSION

4.1. Model fitting and checking

In order to examine the impact of corporate governance elements on sample Ethiopian Banks financial performance panel linear regression model was estimated. The regression analysis enables the researcher to empirically test the proposed hypothesis and to achieve the research objective. Thus, conducting of regression diagnosis tests to select the appropriate model.

Multicollinearity Test

As stated by Pallant (2007), if the value of VIF is less than 10, then no multicollinearity problem exists.

Table 2 multicollinearity test

Variable	VIF	1/VIF
BKS	5.26	0.189968
LIQ	4.78	0.209405
LTD	2.71	0.368566
AQ	2.40	0.417444
BSZ	2.20	0.454657
MEF	2.10	0.475931
LER	2.07	0.482230
ACS	1.23	0.814163
Mean VIF	**2.84**	

Since the variance inflation factor is less than the cutoff point, this indicates that all variables are relevant and multicollinearity is not there since the variance inflation factor (VIF) for each variable is less than the cutoff point 10.

Heteroskedasticity Test

To test the Heteroskedasticity of variables of the research, the researcher used the Breusch-pagan test. The Breusch-Pagan test is used to determine whether or not heteroscedasticity is present in a regression model.

Table 3 Heteroskedasticity Test

Breusch-Pagan / Cook-Weisberg test for heteroskedasticity
Ho: Constant variance
Variables: fitted values of ROA
chi2(1) = 1.20
Prob > chi2 = 0.2725

The figure above shows that the probability value of the chi-square statistic 0.2725 is greater than significance value, indicates a statistically insignificant Chi-square test. This result indicates there is no problem of heteroskedasticity.

Normality Test

Skewness is a measure of the asymmetry of the probability distribution of a random variable about its mean. It represents the amount and direction of skew. The figure below shows the results obtained after performing the Skewness and Kurtosis test for normality.

Table 4 normality test

Skewness/Kurtosis tests for Normality				
			------ joint ------	
Variable	Pr(Skewness)	Pr(Kurtosis)	adj chi2(2)	Prob>chi2
residual	0.2340	0.0332	5.74	0.0567

The probability of skewness which is 0.2340 implying that skewness is asymptotically normally distributed and Prob>chi(2) is 0.0567 which is greater than 0.05 implying its significance at a 5% level. Therefore, according to the Skewness test for normality, residuals show normal distributed. And the shape of histogram of residuals; as we can see from the graph below its like bell shaped so the residuals are normally distributed.
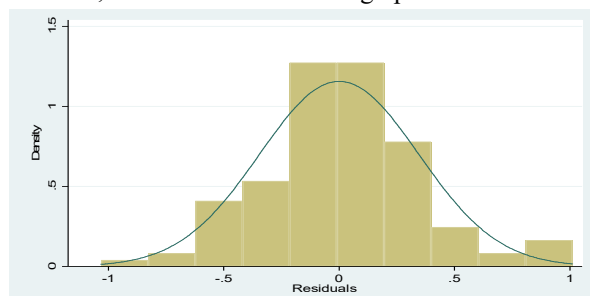

Figure 1 Normality distribution

Stationary Test

In order to identify the Stationarity of the factors for banks in Ethiopia, Levin, Lin & Chu test was used to test the group stationary of each variable. To estimate the long-run variance of the series, xtunitroot by default uses the Bartlett kernel by using of 8 lags as selected by the method proposed by Levin, Lin, and Chu.

Accordingly the probability value of variables is lower than the significance level of 5% and 10%, therefore,

we reject the null hypothesis and conclude that the panel series (variables) were stationary at level and first difference.

Table 5 Levin-Lin-Chu unit-root test

	Statistic	p-value	Order of integration
ROA	-7.8418	0.0000	I(1)
BSZ	-1.7646	0.0388	I(0)
AQ	-1.6353	0.0510	I(0)
MEF	-5.1498	0.0000	I(1)
LTD	-3.1153	0.0009	I(0)
LER	-3.6536	0.0001	I(0)
LIQ	-2.2389	0.0126	I(0)
BKS	-1.6615	0.0483	I(1)
ACS	-1.8308	0.0336	I(0)

Pooled regression

Before applying panel data regression, the first step is to disregard the effects of entity and time and perform pooled regression instead. In this, a usual OLS regression helps to see the effect of independent variables on the dependent variables disregarding the fact that data is both cross-sectional and time series. To check if the result of the pooled regression is appropriate for the panel dataset, confirm that the dummies have no joint effect on the results. If they carry any joint effects then the pooled regression estimates are not viable.

Table 6 Test for pooled Regression

(1) BankID2 = 0
(2) BankID3 = 0
(3) BankID4 = 0
(4) BankID5 = 0
(5) BankID6 = 0
(6) BankID7 = 0
F(6, 102) = 11.01
Prob > F = 0.0000

Here, the null hypothesis suggests that the joint effect of all the dummies is zero. Therefore, the effects of the alternative coming from variations in data due to the distinction of banks do not affect this model. It thus confirms the fact that pooled regression is not free from the joint effects of dummies. Therefore the panel data set here carries the variables due to the distinction between the banks. Resultantly, the pooled regression technique is not a favorable technique for this dataset and consequently moves towards either fixed or random effects panel data regression.

As noted in Brooks (2008), there are two panel data estimator approaches that can be employed in financial research: fixed effects models and random effects models. The results of two models tested in this paper (random effect and fixed effect). Then, diagnostics tools were applied to choose the appropriate model in this study using panel data approach.

Random Effect Model

In a random effect model, the intercepts in the regression equation represent the mean values of cross-sectional intercepts. On the other hand, the error terms represent random deviations of individual intercepts from the mean value. Therefore internalize the effects of 7 bank firms as random effects in the regression equation. Since no joint or alternative effect appears in regression results, generate the effect estimates.

The error variances may be unequal and the problem of heteroscedasticity may be present. To check this, we use Breusch and Pagan Lagrangian multiplier test using the command xttest0. The Breusch and Pegan Lagrangian Multiplier test which helps to identify the presence of heteroscedasticity.

Table 7 Test for random effects

Breusch and Pagan Lagrangian multiplier test for random effects
ROA[ID,t] = Xb + u[ID] + e[ID,t]
Estimated results:
| Var sd = sqrt(Var)
---------+----------------------------
ROA | .5624744 .7499829
e | .0825423 .2873017
u | 0 0
Test: Var(u) = 0
chibar2(01) = 0.00
Prob > chibar2 = 1.0000

In the table above, Breusch and Pagan Lagrangian multiplier test for random effects, under the null hypothesis of there are no random effect, the finding suggested that the researcher cannot reject the null hypothesis that there is no random effect in the data. Therefore, the random effect model is does not significantly able to deal with heterogeneity better than does the pooled OLS. So, the study cannot apply the random effect model.

Since, the pooled regression is not free from the joint effects of dummies and random effect does not significantly able to deal with heterogeneity, as well as significant increase in goodness of fit in the fixed effect model than others; therefore, the fixed effect model is better than the pooled OLS and random effect model.

Fixed Effect

The fixed effect regression is the model to use when researcher wants to control for omitted variables that differ between cases but are constant over time. Fixed effect model allows for heterogeneity or individuality among 7 bank companies by allowing having its own intercept value, but the intercept does not vary over time.

Diagnostics Tests for Fixed Effect

After checking that the fixed effects model is the appropriate model for further analysis the presence of Heteroscedasticity, Cross-Sectional Dependence and Serial Correlation were checked.

Table 8 Heteroskedasticity test for FE

Modified Wald test for groupwise heteroskedasticity in fixed effect regression model
H0: sigma(i)^2 = sigma^2 for all i
chi2 (7) = 52.63
Prob>chi2 = 0.0000

And our significant test rejects the null and indicates that our Fixed-effects model has not free from heteroskedasticity problem.

Because weights are assigned to observations on the basis of the square root of their variances, the FGLS is the most appropriate model when the exact form of heteroscedasticity in the data is not known. It is also resistant to any kind of heteroscedasticity (Martinez et al (2013).

Tests for cross-sectional dependence

To test this hypothesis, we use the xtcsd command after fitting the fixed effect panel data model. We initially use Pesaran's (2004) CD test.

Table 9 CSD Test

Pesaran's test
cross sectional independence = 0.428, Pr = 0.6690

Contemporaneous correlation test carried out in this study with the null hypothesis of no cross-section dependence in residuals. The study confirmed the Pesaran CD test indicated an insignificant p-value of 0.6690, indicating the absence of cross-sectional dependence of the residuals. Here the average absolute correlation is 0.217, which is relatively small value. Hence, there is not enough evidence for suggesting the presence of cross-sectional dependence under a fixed effect specification.

Table 10 BP\LM Test

Correlation matrix of residuals:						
__e1 __e2 __e3 __e4 __e5 __e6 __e7						
__e1 1.0000						
__e2 0.6438 1.0000						
__e3 0.2056 0.2330 1.0000						
__e4 -0.1980 -0.1070 -0.1505 1.0000						
__e5 0.2338 0.3680 0.4199 0.1418 1.0000						
__e6 0.0474 -0.4272 -0.2071 -0.2021 -0.2239 1.0000						
__e7 0.0313 0.0292 0.1588 -0.4031 -0.0192 -0.0993 1.00						
Breusch-Pagan LM test of independence: chi2(21) = 25.315, Pr = 0.2338						
Based on 17 complete observations over panel units						

The null hypothesis in the B-P/LM test of independence is that residuals across entities are not correlated. As shown in the result above the p-values for Breusch-Pagan LM test of independence were Pr = 0.2338, therefore, the study failed to reject the null hypothesis that residuals across entities are not correlated. As a result, the model has no sever cross sectional dependency problem.

Testing for Serial correlation

Because serial correlation in linear panel-data models biases the standard errors and causes the results to be less efficient, researchers need to identify serial correlation in the idiosyncratic error term in a panel-data model. Drukker, D. M. (2003)

Table 11 Wooldridge test

Wooldridge test for autocorrelation in panel data
H0: no first-order autocorrelation
F(1, 6) = 6.427
Prob > F = 0.0444

The null hypothesis of wooldrige test is no first-order autocorrelation, from the above test we have found first-order autocorrelation problem in the fixed effect model.

From the above post estimation tests of fixed effect model, we have found heteroscedasticity and first-order autocorrelation problem in the fixed effect model, since the heteroscedasticity form is not known, the Feasible Generalized Least Squares (FGLS) transforms the variables to get homoscedasticity.

FGLS Estimation

Fixed Effects model then checked for the heteroskedasticity, autocorrelation (Woolridge test for auto-correlation statistic and cross-sectional dependence (BP-LM test) and it is found that the model is suffering from heteroskedasticity and first order autocorrelation problem and application of Fixed Effect Model and Random Effect Model will give inconsistent estimator.

FGLS estimators are consistent and efficient as this method takes into account heteroskedasticity across panels, auto-correlation within panels and cross sectional dependence and can be use when T (time) > N (entity) (Beck and Katz, 1995), which is applicable to this study. FGLS generates estimates that are dependent on the disturbance covariance matrix estimations as well as any estimated autocorrelation parameters (Greene, 2012).

As mentioned above, FGLS estimation is appropriate when there is presence of heteroskedasticity, auto-correlation and cross-sectional dependence in the model. So, discussion of results of FGLS estimation is done here. The regression output in table presented was run by taking ROA as a dependent variable and other financial performances as an independent variable.

Table 12 FGLS

Cross-sectional time-series FGLS regression			
Coefficients: generalized least squares			
Panels: heteroskedastic			
Correlation: common AR(1) coefficient for all panels (0.2996)			

Estimated covariances = 7		Number of obs = 119	
Estimated autocorrelations = 1		Number of groups = 7	
Estimated coefficients = 9		Time periods = 17	
	Wald chi2(8) = 412.60		
	Prob > chi2 = 0.0000		

ROA	Coef.	Std. Err.	P>|z|
BSZ	.0004212	.0280194	0.988
ACS	.0256366	.1386403	0.853
MEF	-.0497466	.0031368	0.000
AQ	-.0683515	.0199432	0.001
LER	.0494441	.0181667	0.006
LIQ	.0121725	.0045105	0.007
BKS	.0910859	.0462248	0.049
LTD	.0089743	.0034222	0.009
_cons	2.988266	.8265021	0.000

Prob > chi2 = 0.0000 showing that the null hypothesis, that all the coefficients jointly zero is rejected. This indicates that the change in dependent variable is well explained by the change in the factor variables of the model.

The result in Table 12 illustrated asset quality, management efficiency, liquidity ratio, loan to deposit and legal reserve (AQ, MEF, LTD, LER, and LIQ) were significant at 1% and bank size (BKS) was significant at 5% level of significance. But, board size (BSZ) and audit committee size (ACS) have no significant impact on the banks financial performance in Ethiopia.

Management efficiency has a negative impact on ROA. It demonstrates the efficiency of management in using the firm's total assets to generate income; the result shows that management efficiency upturn then Return on assets (ROA) shrank by 4.98 percent. The study result is consistent with findings of Reza D. (2018) and Mulualem G. (2015) show negative and significant impact on financial performance of banks. The results of Wondowosen G. (2018) find out significant and positive impact on bank performance.

The coefficient of asset quality (AQ) was negative and statistically significant at 1% (coef. -.06835 and p-value 0.001) and this shows that holding all other factors constant, as asset quality increases by 1%, return on asset decreased by 6.8% and it is statistically significant at 1% level of significant.

Loan to deposit ratio (LTD) was positive significant impact on return on asset at 1% (coef. .0089, p= 0.009). This means LTD has the effect of increasing return on asset by 0.89 percent. Higher loan to deposit ratio indicates, banks has issuing more of its deposit in the form of interest-bearing loans, consequently banks can have generated more profit. But if the ratio is too high banks may default in the repayment of loan. Too low loan to deposit ratio is also a risk for banks. The study result is consistent with findings of Tesfaye B. (2018) and Getahun, K. (2013) and shows that positive and significant impact on banks performance.

The coefficient parameter for legal reserve is .049 with p-value of 0.006; legal reserve ratio significantly and strongly predicts financial performance of banks in terms of return on asset (ROA). It indicates that legal reserve secures customer deposits, safeguard the banking sector and the economies and serves as a motivation for service quality in the banking industry. Legal reserve requirements safeguard market participation, productivity and growth expectations of all commercial banks by using the reserve requirement to ensure that their total bankruptcy is avoided. (Glocker & Towbin, 2012; Bech & Keiser, 2012).

The variable liquidity ratio has a positive coefficient and statistically significant p-value of 0.007, so it is significant at 1% level of significant. It implies that the banks liquidity ratio has a significant impact on the financial performance of banks in Ethiopia. The result revealed that, the increase of liquid asset leads to the enhancement of profitability. The study result is consistent with findings of Ferrouhi (2014), Reza D. (2018), Mulualem G. (2015), and Wondwosen G. (2018) shows that positive and significant impact on commercial banks performance. Whereas, the results of Abdurazak H. (2016) shows that a negative and insignificant association exists between liquidity and profitability.

Coefficient of bank size is .091 and its P-value is 0.049, this means that Bank size (BSZ) has a positive impact on banks financial performance, return on asset (ROA), it implying that large bank size enjoy better

profits than smaller banks. This result is consistent with the finding of Yasser (2011), Harun, A. (2017), Kassa et al., (2013), Fanta A.B., et al. (2013).

5. CONCLUSION AND RECOMENDATION

5.1. Conclusion

The intention of this study was to empirically examine the effect of corporate governance mechanisms on financial performance of Ethiopian banks. In doing so, seven banks operating for the past 17 years (2005 - 2021) were included in the sample for review of documents resulting in observations. The methodology used Panel data in which the multiple regression, FGLS method of estimation was used.

This study used the independent variables: board size, audit committee size, asset quality, legal reserve, liquidity ratio, bank size, loan to deposit, and management efficiency. The dependent variable, financial performance, is measured in terms of return on asset (ROA).

Based on Econometric analysis, the regression analysis indicates that Asset quality and management efficiency negatively and significantly affects the performance of banks measured with Return on Asset. Loan to deposit ratio, liquidity ratio and legal reserve positively affect performance of bank firms measured by return on asset (ROA) in Ethiopia. However, board size, board gender diversity, audit committee size, frequency of board meeting, and bank size have no impact on the bank performance (ROA).

5.2. Recommendations

This study examined the impact of corporate governance on commercial banks' financial performance by taking evidence from selected banks in Ethiopia. On the premise of the findings and conclusions reached, the following subsequent recommendations were forwarded.

Banks should pay greater attention to these significant variables in determining their bank performance. The dimensions of the bank are a crucial factor with a positive contribution to its profitability since attention should tend to increase the whole asset of the bank to boost performance.

The study found that the board of directors of Ethiopian banks is predominantly male, with very limited gender diversity. So, much devotion to be done to improve the gender balances on Ethiopian bank boards.

The dimensions of the bank are a crucial factor with a positive contribution to its profitability since attention should tend to increase the whole asset of the bank to boost performance. And, banks should increase their branches also as their size so as to boost profitability thanks to financial prudence of scale.

The Financial overall performance of banks in Ethiopia may be higher grown, so forth adoption and implementation of corporate governance mechanisms are clearly stated and framed.

The Governor, National Bank of Ethiopia (NBE) should encourage banks to implement good corporate governance practices by enacting rules and regulations.

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