CORPORATE GOVERNANCE AND FIRM PERFORMANCE: AN EVIDENCE FROM VIETNAMESE COMPANIES LISTED ON HANOI STOCK EXCHANGE

QUẢN TRỊ CÔNG TY VÀ HIỆU QUẢ HOẠT ĐỘNG DOANH NGHIỆP: BẰNG CHỨNG THỰC NGHIỆM CÁC CÔNG TY VIỆT NAM NIÊM YẾT TẠI SỞ GIAO DỊCH CHỨNG KHOÁN HÀ NỘI

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Abstract - The paper investigates the relationship between corporate governance and the performance of listed firms in Vietnam. The research data is collected from a sample of 361 companies listed on Hanoi Stock Exchange (HNX) during the period from 2007 to 2015. Pooled Ordinary Least Squares (Pooled OLS) estimation method and Panel Fixed Effects estimation method with robust standard errors are used to estimate the impact of corporate governance on firm performance. The findings reveal that strong board and foreign ownership have significant and positive effects on the performance of firms. However, CEO duality is found to be negatively associated with the firm performance.

Key words - Corporate governance; Firm performance; Vietnamese companies; Hanoi Stock Exchange

Tóm tắt - Bài báo nghiên cứu mối quan hệ giữa quản trị công ty và hiệu quả hoạt động của doanh nghiệp niêm yết tại Việt Nam. Dữ liệu nghiên cứu được thu thập từ mẫu gồm 361 công ty niêm yết tại Sở giao dịch chứng khoán Hà Nội trong giai đoạn từ 2007 đến 2015. Phương pháp bình phương tối thiểu gộp (Pooled OLS) và phương pháp ảnh hưởng cố định (Panel Fixed Effects) kết hợp với việc sử dụng các sai số chuẩn mạnh (robust standard errors) sẽ được sử dụng ước đoán ảnh hưởng của quản trị công ty đến hiệu quả hoạt động của doanh nghiệp. Kết quả nghiên cứu chỉ ra rằng Hội đồng quản trị mạnh (Strong board) và mức độ sở hữu cổ phiếu của nhà đầu tư nước ngoài (Foreign ownership) có ý nghĩa thống kê và tác động tích cực đến hiệu quả hoạt động của doanh nghiệp. Trong khi đó, CEO kiêm nhiệm chủ tịch hội đồng quản trị (CEO duality) được tìm thấy có tác động tiêu cực đến hiệu quả hoạt động của doanh nghiệp.

Từ khóa - Quản trị công ty; Hiệu quả hoạt động của doanh nghiệp; Các công ty niêm yết, Sàn giao dịch chứng khoán Hà Nội

1. Introduction

After the Asian financial crisis (1997-1998) and the global crisis (2007-2008) along with the collapse of a series of businesses due to corporate frauds, effective corporate governance has been a growing concern from many scholars all over the world.

The question of whether or not the effect of corporate governance on firm activities is debated. Several papers indicate that the failure and weakness in corporate governance primarily lead to the global crisis [1-2]. A report of Isaksson & Krikpatrick [3], commissioned by OECD Steering Group on Corporate Governance, highlights that one of the most important causes of economic crisis is the poor governance in terms of risk management, accounting standards, regulatory requirements and remuneration systems.

Regarding firm performance, there are many papers have shown that corporate governance significantly impacts on firm performance [4-14]. They argue that corporate governance helps firms collect more information, therefore make decisions quickly and efficiently. Also, corporate governance will improve board effectiveness and more opportunities to access technical capabilities, outside resources and better managerial capital. Moreover, the effective corporate governance improves the information symmetry. As a result, corporate governance will enhance firm performance.

In Vietnam, according to the report of group of Association of Southeast Asian Nations (ASEAN) Corporate Governance Experts in 2015, Vietnam has the lowest average ASEAN Corporate Governance Score (ACGS) out of six countries participating in the survey. Compared to other Southeast Asian countries' enterprises, listed firms in Vietnam still perform poorly. This leads to the question of whether corporate governance affects firm performance in Vietnam. There are papers investigating the relationship between corporate governance and firm performance. Phan Bui Gia Thuy et al. [15] find that board size has a negative effect on returns on assets (ROA). Vo Hong Duc & Phan Bui Gia Thuy [16] also emphasize that female board members are positively related to firm performance on returns on assets (ROA). Doan Ngoc Phuc & Le Van Thong [17] show that there is a positive relationship of the ownership of Board of Directors and firm performance. Therefore, in this paper, we focus on the question whether corporate governance affects firm performance by using a comprehensive sample of 361 companies listed on Hanoi Stock Exchange (HNX) during the period of 2007-2015. The findings from this paper contribute to the literature by confirming, in Vietnam, the impact of corporate governance on firm performance.

The paper is structured as follows: Section 2 discusses the related literature and the hypothesis development. A description of data and methods is reported in Section 3. Section 4 presents the empirical results. Section 5 will be conclusions and implications from our findings.

2. Literature reviewand hypothesis

Corporate governance and firm performance is one of the topics that has attracted a lot of attention from scholars all over the world [18-20, 15-16]. The works of Bange & Mazzeo [9], Harford & Li [21], Harris & Raviv [22], Pathan [23], Croci & Petmezas [24] have shown that corporate governance can be determined by a number of related factors

such as Strong board, CEO duality and Foreign ownership. In this paper, we focus our attention on investigating the relationship between corporate governance which is represented by the three main variables (Strong board, CEO duality and Foreign ownership) and firm performance.

2.1. Board of directors and firm performance

Board of directors is recognized as the main feature of corporate governance [25]. There are a wide range of board characteristics which have different effects on firm performance in existing literature. Several studies [6-7, 10,13-14] have stated that a bigger Board of directors' size allows gathering greater intellectual capacity, reducing management domain and control, collecting more information, which will impact firm profitability. Nevertheless, Jensen [26] argues that keeping the board of directors small can improve firm performance due to coordination problems and problem solution, which overwhelms the advantages generated by the greater participation of members. In this regard, Haniffa & Hudaib [27], Zabri et al. [28] present an inverse relationship between board size and firm performance. They indicate that having larger board tends to obstruct company's activities in terms of organizing board meetings and reaching at a consensus during the meeting. Hence, by limiting the board size makes it easier to monitor every member, which helps to make decisions quickly and efficiently. In the context of Vietnam, Duc & Thuy [16] find that board size has a negative effect on returns on assets (ROA).

Besides, Fama & Jensen [4], Bhagat & Black [8], Bange & Mazzeo [9] and Pathan [23] argue that independent directors[1] try to maintain their reputation in directorship market. Then, independent directors are more likely to make decisions that can improve firm performance. As a result, Bange & Mazzeo [9], Pathan [23] state that a strong bank board should consist of fewer board members and more independent directors.

Hillman et al. [12] argue that board diversity provides more unique resources and information, that may benefit the decision-making processes, which in turn can enhance the growth of a firm's business. Duc & Thuy [16] emphasize that female board members are positively related to firm performance on returns on assets (ROA). Darko et al. [29] also find the positive relationship between the proportions of female directors on the board with firm performance.

Other studies [10, 30] suggest the positive association between the frequency of corporate board meetings and firm performance. They explain that through meetings, board members determine operational issues through discussing and engaging with each other more frequently. Therefore, meetings enhance the decision-making process, and consequently the performance of the firms.

Regarding board committees, the establishment of different committees will improve board effectiveness [31, 10]. The authors have concluded, firms with more board committees such as audit committees and remuneration committees are related to higher performance.

Based on the arguments presented above, we develop a strong board variable measured by board size, independent directors, female directors, board meetings and board committees and propose the following hypothesis:

Hypothesis *H1*: *Strong board (board size, independent directors, female directors, board meetings and board committees)* positively affects firm performance.

2.2. CEO duality and firm performance

Chief executive officer (CEO) duality means that chief executive officer also holds the function of the chairman of the board. According to Faleye [32], CEO duality is more beneficial for CEOs to hold the decision-making rights which gives the flexibility to understand and respond to the market change without constrained top executive. However, in agency theory, CEO duality is shown to reduce the firm performance due to the moral hazard [33]. Daily and Dalton [34] and Coles et al. [35] also report that CEO duality has a negative effect on financial performance. As Tuggle et al. [36] and Rashid [37] find that CEO duality inhibits the board's ability to implement the function of corporate governance.

Based on the arguments presented above, we propose the following hypothesis:

Hypothesis *H2*: *There is a negative relationship between* CEO duality *and firm performance.*

2.3. Foreign ownership and firm performance

Azutoru et al. [38] reveal the significant and negative correlation between the proportion of foreign shareholders and the firm performance. Conversely, Trinh & Vy [39] find out different effects of foreign ownership and squared foreign ownership on ROA, which indicates that there is U-shape correlation between the proportion of foreign shareholders and the profitability of Vietnamese firms. Foreign ownership initially has a negative effect on the firm performance but when foreign ownership reaches or is above 25.7%, this effect becomes positive. These results tend to imply that holding low level of equity, foreign investors are limited in monitoring role and showing their advantages; however, they will boost firm profitability when they have enough equity proportion due to effective monitor function, information disclosure, accounting practices and useful knowledge and technology.

Mohd [40] suggests that foreign shareholders play an important role in managing and reducing agency cost. Foreign ownership corporations help firms have more opportunities to access technical capabilities, outside resources and better managerial capital. Moreover, foreign shareholders improve the information symmetry because they contribute to reducing the issues of adverse selection and hidden actions in management. Thus, a number of papers such as works [41-42] have shown that foreign ownership (with many advantages) influences firm performance positively

The arguments presented above suggest the following hypotheses:

Hypothesis *H3*: *There is a positive relationship between foreign ownership and firm performance*

[1] Non-employee directors

3. Data and econometric methods

3.1. Data and sample

In order to test the hypotheses, we collect the data on firm performance and control variables from companies listed on Hanoi Stock Exchange (HNX) during the period of 2007-2015. The data is collected from Fiingroup[2] (previously StoxPlus), which is the Vietnam's leading integrated service provider of financial data, business information and industry research. Data on corporate governance is collected manually from the individual firm's annual reports that are available on Mint Global database of Bureau Van Dijk. Also, financial institutions are excluded from the sample due to the difference in the capital structures and operations' requirements. After screening criteria and deleting observations with missing values, we end up with the sample of 361 companies listed on Hanoi Stock Exchange (HNX) for the period of 2007-2015.

3.2. Methods

To examine our hypotheses on the impact of corporate governance on firm performance, we carry panel data regression of the corporate governance, *GOVERNANCE*, on firm performance, *PERFORMANCE*. We also control for firm-specific level, industry fixed effects and year fixed effects. Specifically:

$$PERFORMANCE_{i,t} = \beta_0 + \beta_1 GOVERNANCE_{i,t-1} + \beta_2 CONTROLS_{i,t-1} + \gamma_j + \delta_t + \varepsilon_{i,t} \quad (1)$$

where as:

3.2.1. Dependence variables (PERFORMANCE)

In this research, firm performance is represented by two different approaches: accounting-based measure (Return on Assets) and market-based measure (Tobin's Q), which are widely used to measure firm profitability in the literature review [43-46].

- Return on Assets (ROA) is recognized as an important measure of a firm's earnings performance. ROA is defined as the firm's net income over the total assets. It illustrates how effectively firm uses its assets to generate earnings.

- Tobin's Q (TOBIN'S Q), which equals the sum of the market value of stock and the book value of debt divided by the book value of total assets, is used as another measure of firm performance based on market. It reflects the relationship between market valuation and intrinsic value as well as market's expectations on future earnings of firm.

3.2.2. Independence variables (GOVERNANCE)

Previous studies have shown that the effectiveness of corporate governance can be determined by a number of related factors such as Strong board, CEO duality and Foreign ownership, for example works by [9, 21-23]. Therefore, in this paper corporate governance is represented by the three main variables:

Strong board (STRONGBOARD) measures the power of a board of directors. It is the combination of five individual board characteristics which are represented by five dummy variables: Board size (the dummy variable equals 1 if the number of board members is less than the median of sample, otherwise 0), Independent directors (the dummy variable equals 1 if the number of independent directors is higher than the median of sample, otherwise 0), Female directors (the dummy variable equals 1 if the number of female directors is higher than the median of sample, otherwise 0), Board committee (the dummy variable equals 1 if the number of board committees is higher than the median of sample and 0 otherwise), and Board meetings (the dummy variable equals 1 if the number of board meetings is higher than the median of sample and 0otherwise). In other words, STRONGBOARD variable is calculated by summing five binary variables: Board size, Independent directors, Female directors, Board committees, Board meetings. The maximum value for a strong board index is 5, and a higher index represents the stronger the board.

- CEO duality (CEO DUALITY) implies that the position of the chairman of the board is held by CEO. It is measured as a dummy variable taking on the value of one if the CEO also holds the position of the chairman of the board, and zero otherwise.

- Foreign ownership (FOREIGN OWNERSHIP) measures the level of foreign investors holding firm's equity. It is calculated by the percentage of shares held by all foreign investors in the capital structure of companies.

3.2.3. Control variables (CONTROLS)

Four control variables which may affect firm performance are added to the sample, including: FIRM SIZE measured by natural logarithm of total assets, LEVERAGE measured by ratio of total debts to total assets, SALES GROWTH measured by the proportion of an increase in company's sales and FIRM AGE measured by the number of operating years since establishment.

Winsorizing at 1% percentile and 99% percentile is used to limit the effect of outliers on regression results. In the model (1) fixed industry effect (γ_j) and fixed year effect (δ_t) are employed -to control the dominant impacts of year and industry on the relationship between corporate governance and firm performance. Moreover, all independent variables are used with lagged values to reduce the effect of endogeneity.

Besides, robust standard errors are employed to solve the problem of hetero skedasticity and are estimated by industry to solve the problem of autocorrelation [47].

4. Regression results

4.1. Descriptive statistics

There are 361 listed companies in the sample over the period of 9 years (2007-2015). Table1 below illustrates the summary of the descriptive statistics of Independent variables (Corporate Governance), Dependent variables (Firm Performance) and Controls variables in the model.

As can be seen from Table 1, strong board variable ranges from a minimum value of 0 to a maximum value of

[2] http://fiingroup.vn/

4 and there is no company having the possible maximum value of 5. Its mean value is 1.077 which implies that in this period, the power of board of directors in firms listed in HNX is considerably low. Besides, the CEO duality variable has an average value of 0.428 while the highest value is 1. It reveals that there are nearly half of companies in the sample having CEOs who also hold the chairman position. Meanwhile, the mean value of the foreign ownership variable is only 0.032, implying that there is a very small amount of foreign capital invested in firms in Vietnam during this research period.

The return on assets (ROA) ranges from a minimum value of -0.145 to a maximum value of 0.405 and the mean equals to 0.091, indicating that the gaps of firm profitability between listed firms are large. Also, the Tobin's Q ranges from the minimum value of -0.376 to the maximum value of 7.011 and the average value is 0.948. This shows that the market's expectation of future earnings is relatively low for Vietnamese listed companies. In addition, Table 1 also presents the the summary of the descriptive statistics of control variables, including: FIRM SIZE, LEVERAGE, SALES GROWTH, and FIRM AGE.

Table 1. *Descriptive statistics of variables*

Variables	***N***	***Mean***	***Median***	***Standard Deviation***	***Min***	***Max***
Corporate governance variables (Independent variables)						
STRONG BOARD	2,601	1.077	1	0.84	0	4
CEO DUALITY	2,897	0.428	0	0.495	0	1
FOREIGN OWNERSHIP	3,250	0.032	0.002	0.08	0	1
Firm performance variables (Dependent variables)						
ROA	2,800	0.091	0.080	0.081	-0.145	0.405
TOBIN'S Q	3,020	0.948	0.909	0.565	-0.376	7.011
Control variables						
FIRM SIZE	3,030	26.149	26.084	1.337	23.501	30.583
LEVERAGE	3,029	0.233	0.205	0.201	0	0.750
SALES GROWTH	2,777	0.312	0.114	1.126	-0.929	9.261
FIRM AGE	2,862	18.940	15.000	14.049	0	59

(Source: Authors' calculations)

4.2. The impact of corporate governance on firm performance

Table 2 presents the regression results of two different regression analyses, Pooled OLS and Panel fixed effects with robust standard errors. These models are used to estimate the impact of corporate governance on firm performance. Particularly, corporate governance is measured by the three main variables: (i) Strong board; (ii) CEO duality; and (iii) Foreign ownership. ROA and Tobin's Q are proxies for firm performance.

From Table 1, while STRONGBOARD variables are found to be negatively and insignificantly related to ROAs, STRONG BOARD variables are positive and significantly related to Tobin's Q. These findings show that greater power of board of directors exhibits higher firm performance under market-based measure.

The negatively and statistically significant coefficients of the *STRONG BOARD* variables when regressing on Tobin's Q partly support the hypothesis **H1.** Accordingly, the strength of the board (board size, independent directors, female directors, board meetings and board committees) will positively affect firm performance.

It can be clearly seen that *CEO DUALITY* has the significant and negative relationship with ROA and Tobin's Q when we use 2 difference regressions Pooled OLS and Panel Fixed Effects. It means that when CEO also holds the function of the chairman of the board, the firm performance tends to be reduced. The results, again, support our hypothesis ***H2*** and suggest that *There is a negative relationship between* CEO duality *and firm performance.*

The results in Table 2 also indicate that FOREIGN OWNERSHIP is positively and significantly related to firm performance measured by both ROA and Tobin's Q.

These findings show that the higher proportion of foreign ownership, the better firm performance. This result is in line with many prior studies (Dwivedi & Jain, 2015; Mohd, 2015; Azutoru et al., 2017). In the context of Vietnam foreign investors may help Vietnamese listed firms to innovate and follow the modern and flexible corporate governance framework according to international standard. In addition, foreign ownership plays an important role in promoting transparency in the information system of the board, which is indispensable to minimize agency problem in order to increase firm performance.

Foreign ownership is also an incentive to help firms apply advanced technology so as to increase labor productivity.

Therefore, the direct participation of foreign shareholders in corporate governance activities will not only improves the management capacity and competitiveness but also increase the reputation and credibility of firms in comparison with those having mere domestic capital. This finding also supports hypothesis ***H3*** that the higher foreign ownership levels, the better the firm performance.

Table 2. *Corporate governance and Firm performance*

VARIABLES	Dependent variable: ROA (1)		Dependent variable: Tobin's Q (2)	
	Pooled OLS	**FEM**	**Pooled OLS**	**FEM**
STRONG BOARD	-0.00188	-0.00269	**0.03844*** **	**0.03073***
	(0.429)	(0.234)	**(0.005)**	**(0.051)**
CEO DUALITY	**-0.00843****	**-0.00964****	**-0.04352***	**-0.03776***
	(0.036)	**(0.011)**	**(0.061)**	**(0.057)**
FOREIGN OWNERSHIP	**0.11233*****	**0.06296****	**0.29866****	**0.22933***
	(0.000)	**(0.022)**	(0.029)	**(0.052)**
FIRM SIZE	-0.00848***	-0.00130	-0.01834*	0.01921
	(0.000)	(0.497)	(0.076)	(0.129)
LEVERAGE	-0.03060***	-0.06307***	-0.19252***	-0.31798***
	(0.008)	(0.000)	(0.004)	(0.000)
SALES GROWTH	-0.00628**	-0.00386	-0.03336**	-0.02022
	(0.021)	(0.178)	(0.016)	(0.114)
FIRM AGE	0.00063***	0.00044***	-6.31e-06	0.00103
	(0.000)	(0.002)	(0.994)	(0.197)
Constant	0.32036***	0.14756***	1.41257***	0.82199***
	(0.000)	(0.003)	(0.000)	(0.009)
Observations	1,624	1,624	1,901	1,901
R-squared	0.058	0.152	0.021	0.214
Industry fixed effect		YES		YES
Year fixed effect		YES		YES

Robust standard errors in parentheses

*** p<0.01, ** p<0.05, * p<0.1

(Source: Authors' calculations)

5. Conclusion

This study investigates whether corporate governance affects firm performance by using a comprehensive sample of 361 companies listed on Hanoi Stock Exchange (HNX) during the period of 2007-2015. After controlling for firm-specific level, industry fixed effects and year fixed effects, the empirical results indicate that there is a significant relationship between corporate governance and firm performance. More specifically, strong *board positively affect firm performance. Also,* foreign ownership positively affects firm performance. While CEO duality negatively impacts firm performance. In Specifically, strong board positively affects firm performance. Also, foreign ownership positively affects firm performance. While CEO duality negatively impacts firm performance. In general, the results have supported our proposed hypotheses.

The findings of the paper contribute important implications. Firstly, the findings help policy makers, businesses and investors understand the consequences of corporate governance on firm performance. Accordingly, they should pay more attention to the strength of the board in order to enhance firm performance. A strong bank board should consist of fewer board members and more independent directors, more female board members, frequent board meetings and more board committees. Secondly, CEO duality is also found to reduce the firm performance. Therefore, separating two positions of board chairman and CEO will help firms increase board's independence and improve board's ability to implement the function of corporate governance; thereby enhances firm performance. Finally, foreign ownership has a positive effect on the performance of listed firms in Vietnam. In other words, the more shares held by foreign investors, the more profitability the firms will have. Foreign investors contribute not only to changing and standardizing the corporate governance system but also help firms have more opportunities to access technical capabilities, outside resources and better managerial capital. Moreover, foreign shareholders improve the information symmetry. Therefore, policy makers, businesses and investors should attract more capital from foreign investors in order to increase firm performance.

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