

How Do Board Characteristics Influence Business Performance? Evidence from Non-life Insurance Firms in Zimbabwe

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Abstract: The purpose of this study was to contribute to the corporate governance literature by establishing the relationship between board characteristics and corporate performance within the non-life insurance firms in Zimbabwe. The study sought to provide some insights on corporate governance since the phenomenon is relatively an emerging discipline in Zimbabwe. The paper sought to complement other corporate governance studies that were conducted in other environments by producing evidence on the phenomenon from a developing country context. A quantitative research approach was adopted and respondents were selected through a stratified random sampling. The results of the study confirm that board characteristics (board composition, diversity, and size) exhibit a statistically significant positive predictive relationship with the performance of non-life insurance firms measured by gross premium written and customer retention. However, CEO/Chairman duality showed a negative relationship with business performance. Non-life insurance companies need to be cognizant of board characteristics in order to improve their performance. Moreover, the findings in this research has practical relevance for the selection process of directors as it highlights the importance of having a sizeable number of board members as well as an appropriate mix of competences and qualifications on the board. Although corporate governance is has been extensively researched, there is limited study in this area from a developing country like Zimbabwe with relatively less developed capital markets. It would be wrong to assume that the findings found in other countries can apply here because the conditions are different.

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1. Introduction

Enough evidence exists to prove that corporate governance in the Zimbabwean insurance industry is one of the worst in Africa. For instance, ZIMRE Holdings Limited's non-life insurer SFG Insurance collapsed in 2013 and investigations by IPEC revealed that the company had a huge negative solvency and its capital base was falling short of the minimum capital threshold. Much evidence also pointed to substandard corporate governance structures. Another case worthy noting is that of Champions Insurance Company, which has been fingered in the Air Zimbabwe insurance scandal where tender procedures were not being followed. Another insurance giant, SFG insurance company collapsed and totally went under in 2013. Further, the Insurance and Pensions Commission (IPEC) of Zimbabwe recently deregistered Global Insurance Company, Jupiter Insurance Company and Excellence Insurance Company as a result of poor corporate governance, in spite of booming insurance business in Zimbabwe (IPEC, 2013).

The scandals highlight how board members can abuse positions to influence certain transactions in their favour, thereby undermining the performance of the firms. Navistar insurance brokers has been, since 2009, siphoning money from Air Zimbabwe through purported insurance programmes which are now emerging to be fraudulent. The company's four directors have since been arrested and await sentencing together with their accomplices from Air Zimbabwe (Matambanadzo, 2014).

Given the apparent central and integral role of the boards of directors in the day-to-day running and management of contemporary corporations, this paper seeks to analyse the impact of board characteristics on performance of non-life insurance companies in Zimbabwe. Particular reference is made to the insurance sector because the majority of corporate governance pronouncements, which are sector wide, do not address the specific concerns of the insurance sector. Furthermore, majority of these corporate governance pronouncements and codes are concerned primarily with the single agency relationship between company directors and shareholders, rather than accounting for the broad range of principals that are features of the insurance companies. Thus, the distinctive characteristics of insurance companies imply the need for distinctive corporate governance arrangements for this sector.

Although corporate governance is has been extensively researched, there is limited study in this area from a developing country like Zimbabwe with relatively less developed capital markets. Most of studies have been conducted in western and Asian countries. For example, in the USA (Bauer, Eichholtz and Kok, 2009, Erkens, Hung and Matos, 2012), in Malaysia (Yasser *et al.*, 2011), in the Netherlands (Rovers, 2011) and in Australia (Christensen *et al.*, 2010). It would be wrong to assume that the findings found in these countries can apply here because the conditions are different. It is against this identified research gap that this study

therefore seeks to examine the relationship between key board characteristics and the performance of Zimbabwean non-life insurance companies.

Following this discussion, the main purpose of this study therefore is to establish the relationship between board characteristics and corporate performance in non-life insurance firms.

This study contributes to existing knowledge base and understandability on the impact of board characteristics on firm performance, since corporate governance by its nature is relatively an emerging discipline in Zimbabwe. It is hoped that the recommendations from this research will help directors and owners within the insurance sector to recognize the significance of corporate governance in enhancing performance of their firms. The rest of the article is presented as follows: a review of literature and a conceptual framework as well as the hypotheses development are presented. Thereafter, the research methodology, the results and the discussion of results are provided. The discussion on the managerial implications, limitations and avenues for future research studies, are to form the last sections of the study.

2. Literature Review

2.1. Corporate Governance

Corporate governance, as a concept is difficult to define, as what constitutes it varies from country to country due to differences in culture, legal systems and historical developments (Wong, 2011). However, there can be no dispute that effective accountability to all shareholders, including the diverse interests of other stakeholders like lenders, employees and government is the essence of corporate governance (Lawal, 2012). Shah, Butt and Saeed (2011) describe it as the way in which an organization is administered, directed or controlled. The authors proceed to state that corporate governance provides the set of rules and regulations that affect how corporations are run and managed, through specifying the distribution of responsibilities and rights among stakeholders. Relatedly, Lawal (2012) asserts that corporate governance involves a set of relationships between a company's management, its board of directors and stakeholders that provides the structure through which the objectives of the company are set and the means of attaining those objectives.

This study is informed mostly by the agency theory and a discussion of the theory follows below.

2.2 The Agency Theory

The agency theory, premised on the contractual relationship between principals (shareholders) and agents (management), suggests that the separation of corporate ownership and control potentially leads to self-interested actions by managers.

According to Jensen and Meckling (1976), a critical notion about the agency theory is that managers, who are contracted to perform services on behalf of the shareholders, are self-interested and unwilling to sacrifice their personal interests for the interests of the shareholders. These self-interests result in an in-born conflict of interest amongst the shareholders and management, as managers in general act for their own interests and they do not take the best probable action for both the public and shareholders (Agrawal and Chadha, 2005; Daily, Dalton and Canella, 2003). This study submits that management may actively maximize their self-interest at the expense of organizational profitability.

2.3 Board Characteristics

A corporate board is delegated with the task of monitoring the performance, and activities of the top management to ensure that latter acts in the best interests of all the shareholders. The relationship between various board characteristics such as the board size, composition and firm performance has been of enormous interest to some researchers for the past decades (Adams *et al.*, 2010). Evidence points much to the thinking that the failure of financial services entities to meet stakeholders' expectations is due to poor governance. This has been observed in incidences of inadequate internal controls and dominance of individuals resulting in inefficiencies and inflated costs of operations. Such was the case at Navistar Insurance Brokers, Altfin Insurance, Jupiter Insurance, Standard Fire and General Insurance and Global Insurance Company (Insurance and Pensions Commission, 2014). The subsequent sections will examine the key variables of the study namely the independent variables (board size, board composition, CEO duality and board diversity) and the dependent variable (corporate performance). The board composition characteristics considered in this research are board size; CEO duality; board diversity and board composition.

2.4 Board Size

Board size refers to the total number of directors on a firm's board. Determining the ideal board size for organisations is very important because the number and quality of quality of directors determines the corporate performance of such firms. The underlying economics of this is that as the board size increases, it will reach a point of diminishing returns at which there will be negative impacts on the functioning of the board, for example when communication and coordination become an arduous and time consuming process for the many directors on a large board (Liu and Fong, 2010).

To date, there is no universally accepted standard to guide the number of directors a firm can have. According to Chinese corporate law, the number of directors on the board may be between five to nineteen people (Liu and Fong, 2010). However, Lawal (2012) recommended a minimum of seven and a maximum of nine board members. Yuanto, (2003) also suggested board size of five board members. This was

also supported by Yammesri and Herath (2010) who suggest that the board of directors can do their tasks effectively when the board size is not more than seven or eight members. Some practitioners and academics strongly believe that board size is a function of factors which include age of the firm, its size and the industry to which it belongs (Lawal, 2012).

2.5 Board Composition

Board composition is the proportion of non-executive directors on the board compared to executive directors. Executive directors are inside directors who participate directly in the day to day management of the company. Independent outside directors, on the other hand are directors who provide the desired outside eye in ensuring that the shareholders' interests are safeguarded (Lawal, 2012). Generally a director who is a full time employee of a company is deemed to be an inside director, while a director whose primary employment is not with the firm is deemed to be an outside director (Tricker, 2009).

This distinction is derived from the extent of their participation in firm management. Inside directors are those directors that are also managers and or current offices in the firm while outside directors (also known as external or non-executive directors); there are directors who are affiliated, and others who are independent. Affiliated directors are non-employee directors with personal or business relationship with the company while independent directors are those that have neither personal nor business relationship with the company (Bhakat and Black, 2002). In order to effectively fulfill their monitoring role, boards of directors must have some degree of independence from management (Dahya and McConnell, 2007).

Board independence is by and large influenced by how it is composed. A board is said to be independent if made up of more non-execute directors than executive directors. The independent outside director brings to fruition the desired neutrality and minimise bias in the board processes (Bhakat and Black, 2002). The global economy appears to have become caught up in what might be described as 'outside director's euphoria' (Dahya and McConnell, (2007). The authors contend that in large measure, this presumption rests on faith rather than evidence. Whilst most of the codes for best practices have emphasised the need for mix directorship with greater non-executive representation, empirical evidence remains conflicting with respect to whether such inclusion significantly induces firm performance.

2.6 CEO Duality

A crucial monitoring mechanism based on the agency perspective is the separation of the roles of CEO from chairman. CEO duality exists when a firm's CEO also serves as the Chairperson of the board of directors (Kang, 2010). CEO duality, by definition, is counterintuitive to the tenets of agency theory if the role of the board is to monitor the CEO and other agents (Carty, 2012). This is typical of CEOs with

long tenure and is common in the United States with approximately 80 percent of the Standard and poor's 500 companies employing a single person to serve in both roles (Carty, 2012). The proponents of this duality role believe that allowing just one person to function as the chairperson and CEO will provide a beneficial platform that is not potentially detrimental. For example the greater levels of information and knowledge possessed by a joint CEO/Chairperson will enable him to better manage and direct the board's discussions and agenda. Others have suggested that this duality role is more efficient and therefore more sensible form of governance (Adams, 2009).

2.7 Board Diversity

Board diversity is premised on two main corporate governance theories, namely stakeholders and resource dependency theories (Kang, 2010). Carpenter and Westphal (2010) assert that for a board to be diverse it ought to have individuals not necessarily from different cultural It is argued that demographically diverse directors are more independent, as they are less likely to be part of an 'old boys' network (Carter, Simkins and Simpson, 2003).

2.8 Corporate Performance

How to measure business performance still remains a debatable subject amongst business practitioners, consultants and academics as organizations can generally use objective and subjective measures to assess their success. Objective measures mostly encompass comparing corporate performance with financial measures, while subjective measures refer to personal perceptions about business performance (Reijonen, 2008). Traditionally, business success has been assessed by financial measures like, return on assets employed, return on sales, growth in revenues, Tobin's Q, return on investment, return on assets, sales revenue, return on equity, earnings per share, net profit margin, stock returns and economic embedded value, market share (Chenhall and Smith, 2007; Reijonen, 2008). The use and reliance on financial measures of business performance has been supported by various authors. For instance, Verbeeten and Boons (2009) argue that financial measures are subjected to internal controls which make them reliable; they are also reported externally and hence are subject to public scrutiny.

On the contrary, Chow and Van der Stede (2006) criticise the traditional financial measures of performance for being flawed by the use of historical data, which is not reliable in assessing corporate performance. Traditional financial measures are difficult to obtain and the organisations have a tendency to conceal some financial information that is useful in assessing their performance (Salameh, Abu-Serdaneh and Zurikat (2009; Jusoh, 2008; Tang and Zhang, 2005). Due to these shortcomings of financial measures, many companies are now implementing broader based measures of their performance that include the non-financial measures for example market share, customer satisfaction, employee turnover and new product

development (Verbeeten and Boons, 2009; Wilkes, 2004). Jusoh (2008) argues that the strength of non-financial measures lies in their ability to provide insight into business processes and outcomes to be better predictors of future corporate performance than the historical financial measures.

Amongst the so many non-financial measures of corporate performance; gross premium written, product innovation and quality; customer retention; quality and quick decision making are the measures adopted in this study. Apart from the arguments already put forward in favour of non-financial measures, the chosen measures of corporate performance are more specific to the business processes in the non-life insurance sector and data on these is not sensitive and therefore respondents will be eager to respond and participate. As advised by Chow and Van der Stede (2006) and Atkinson and Brown (2001), the subjective approach was used in this study to measure corporate performance of non-life insurance firms. These include gross premium written and customer retention.

3. Research Methodology

The study adopted a quantitative approach to collect data from the non-life insurance firms in Zimbabwe that were stratified into strata namely: insurers, reinsurers and broking companies operating in Harare as this is where most firms are headquartered. From these strata board 170 members were randomly selected. Self-administered questionnaires were sent through the email or drop-off method.

3.1 Reliability and Validity

The internal consistency reliability of the questionnaire was tested by computing the Cronbach’s Alpha coefficient. The reliability of each scale was checked. As indicated in Table 3, all the scales in the study yielded an alpha value greater than 0.7, board size (0.746), board composition (0.733), CEO duality (0.856) and board diversity (0.801), which means that the scales for all the constructs were reliable. Table 1 depicts the internal reliability statistics of the scales used in this study.

Table 1. Reliability statistics

Variables	Number of Items	Cronbach's Alpha value
Board Size	5	0.746
Board Composition	6	0.733
CEO Duality	5	0.856
Board Diversity	7	0.801

A pilot study was undertaken to ensure face and content validity of the questionnaire and check that it was understandable, acceptable and captured the gist of the

research. The feedback gave an opportunity to modify and improve the questionnaire by making adjustments to some questions that lacked clarity.

4. Results and Discussion

4.1 Sample Demographics

A total of 170 questionnaires were distributed and 140 of them were completed, marking an overall response rate of 82.4%, with the respective response rates for each strata as shown in Table 2. The gender profile of the respondents revealed that male respondents (n=84 constituting 60%), were more than female respondents (n=56 constituting 40%) of the total respondents. In terms of the educational background of the respondents, the results indicates 112 were degree holders, while 12 were holding post graduate degrees and 16 were diploma holders. Responses regarding the current position were as follows: executive directors (n=36; 26%), CEOs (n=32; 23%), non-executive directors (n=24; 17%), independent directors (n=24; 17%), and board chairmen (n=16; 11%), doubling as CEOs and chairmen (n=8; 6%),

4.2 Correlation Analysis

Before testing the effect of corporate board characteristics on the performance of insurance companies, Pearson's correlation analysis was carried out to test the direction and strength of relationships between these variables. The Pearson's correlation coefficient ranges from +1 for a perfect positive correlation to -1 for a perfect negative correlation (Welman, Kruger and Mitchel, 2005). Table 2 depicts the correlation results.

Table 2. Board Characteristics and Business Performance

Factors	BS	BC	CD	BD	BP
Board size (BS)	1				
Board composition (BC)	.452*	1			
CEO duality (CD)	.280*	.090*	1		
Board diversity (BD)	.491*	.377*	.198	1	
Business performance (BP)	.331*	.286	-.379	.473*	1

** Correlation is significant at the 0.05 level.

The results depicted in Table 3 demonstrate significant weak but positive correlations between the three characteristics of corporate performance: board composition (r= 0.286, p<0.01), board diversity (r= 0.473, p<0.01) and board size (r=0.331, 0.01) However, CEO duality (r= -0.379, p<0.01) showed a weak and negative association with business performance.

Similar findings about the positive correlations between business performance and corporate governance characteristics (board composition, diversity and size) are reported by authors namely Yasser, Enterbang and Mansor (2011), Rovers (2011) and Abidin, Kamal and Jusoff (2009). The result showing a negative association between CEO duality and business performance is consistent with Brown and Robinson (2004) and Bokpin, Kyereboach and Aboagye (2006).

4.3 Regression Analysis

After testing correlations between the variables, the study further carried out a regression analysis because as correlations analysis only measure the magnitude and direction of a correction but do not to establish the predictive relationship between variables. Regression analysis was conducted to ascertain the predictive power of corporate governance characteristics (board diversity, composition, size and CEO duality) on business performance. Table 3 presents the regression results showing the predictive power of each factor on business performance.

Table 3. Regression analysis between corporate governance characteristics and business performance

Dependent variable: corporate performance				
Predictor variables	Std error	Beta	t-value	p-value
Constant	11.43		2.35	0.000
Board size	0.028	-0.15	1.12	0.031
Board composition	0.023	0.21	1.11	0.033
CEO duality	0.010	-0.37	2.76	0.021
Board diversity	0.037	0.17	3.01	0.019

R =63.23; R-squared = 65.05; Adjusted R-squared =60.01; F = 22.05; ** significant at p<0.01

The results depicted in Table 3 indicate that the four characteristics of corporate governance had an adjusted R-squared value of 60.01 which demonstrates that the corporate governance characteristics explained about 60% of the variance in business performance. Table 4 also shows the results of the beta coefficients. The results reveal that board size measured by the number of directors has a statistically significant negative relationship with business performance ($\beta = -0.15$, $p < 0.05$), thus confirming the hypothesis 1 that a smaller board has a positive influence on business performance of non-life insurance firms in Zimbabwe. The result is consistent with prior studies (Yasser *et al.*, 2011, Abidin *et al.*, 2009, Bokpin *et al.*, 2006).

The relationship between board composition and business performance is positive and significant ($\beta = 0.21$, $p < 0.05$). This is a demonstration that from the sampled non-life insurance firms in Zimbabwe, there is a positive relationship between an organisation's performance and the presence of non- executive directors who sit on

the board (Yasser *et al.*, 2011). The outcome is in agreement with previous studies (Bhagat and Black, 2002, Sanda *et al.*, 2006). Therefore hypothesis 2 stating that board composition positively impacts on business performance of non-life insurance firms in Zimbabwe is supported.

The results also show that CEO/Chairman duality has a negative influence on business performance as the beta coefficient is -0.37. This shows that the sampled non-life insurance companies in Zimbabwe are in favour of having one person being a board chair and the other being the chief executive officer. The implication is that the performance of sampled non-life insurance firms in Zimbabwe improves if two people occupy the positions of the board chair and the chief executive. The result is in agreement with previous studies (Christensen *et al.*, 2010, Bokpin *et al.*, 2006, Brown *et al.*, 2004). Therefore hypothesis 3 that states that CEO/Chairman duality negatively influences business performance of non-life insurance firms in Zimbabwe accepted.

The relationship between board diversity and business performance as shown in Table 4 is positive and statistically significant ($\beta=0.17$, $p<0.05$). This implies that the sampled short non-life insurance firms in Zimbabwe need a well-diversified board because board members of different gender, education background, and work experiences share their different ideas to improve business performance. The outcome is consistent with a study by Rovers (2011). Hypothesis 4 stating that board diversity positively impacts on the performance of short term insurance firms in Zimbabwe is accepted.

5. Recommendations

The findings that about the influence of board size, board composition, CEO duality and board diversity influence corporate performance have relevance for managers and owners, as well as researchers and academics. Management should be cognizant of how board configurations and leadership structure may impact their corporate performance. Thus, it is of paramount importance that firms should take a serious consideration into the size of their boards as results show that board size affects effectiveness of the board above some desired threshold. Findings of this study reveal an optimal board size of between 7 and 9 members is the most ideal. Furthermore, the study shows that female board members are not just mere figures, but rather contribute significantly to board strategic decision making, gross premium written, customer retention and product innovation. Accordingly, firms should include women as well to be part of their board of directors.

Additionally, the finding that the proportion of outside directors and CEO duality were negatively related to corporate performance has practical implications as well. From the shareholders' standpoint, having greater outsider representation and

avoiding duality is an effective way to monitor management. Moreover, to effectively fulfill their monitoring role, boards of directors must have some degree of independence from management. Indeed outside directors can play a significant role in arbitrating in disagreements between internal managers and help to reduce agency problems. The recommendation is that a board should ideally have more independent outside directors than inside executive directors. The independent outside directors bring to fruition the much desired neutrality and eliminates bias in the board processes. The study, just like the Cadbury Report, recommends having at least three outside directors.

Another crucial monitoring mechanism based on the agency perspective is the separation of the roles of CEO from chairman. The practice of CEO duality is not advisable because it threatens the independence of the board. The study recommends that the roles of the CEO and chairman be taken by two different people. It is also recommended that non-life insurance companies should have boards that are up made of individuals not necessarily from different cultural backgrounds but those from different academic orientations, which then fosters collaboration. Thus diversity of boards should represent both demographic and qualifications of the members.

6. Conclusions

The major objective of this study was to establish the relationship between board characteristics and corporate performance with particular reference to non-life insurance firms. The results of the study confirm that board characteristics (board composition, diversity, and size) exhibit a positive predictive relationship with the performance of non-life insurance firms. However, CEO/Chairman duality showed a negative relationship with business performance. The results lend support to previous streams of research, which demonstrate that board characteristics have a positive relationship with business performance. Therefore, non-life insurance companies need to be cognizant of board characteristics in order to improve their performance. Moreover, the findings in this research has practical relevance for the selection process of directors as it highlights the importance of having an appropriate mix of competences and qualifications on the board.

7. Limitations and Avenues for Future Research

Although this study has provided some useful information about the relationship between board characteristics and corporate performance measured by qualitative indicators, the results of study may be interpreted with caution because of the following limitations. The use of structured questionnaires to collect data limited the depth of information received from the board members. The reliance on the

subjective views of corporate performance is a limitation in the study in terms of generalisation of the results to other companies because they could have different views about board characteristics and corporate performance.

In addition, considering that the sample population was drawn from Harare, and taking into account that there are several non-life insurance companies operating in other provinces whose conditions might be different from those found in Harare, the generalisation of the results therefore needs to be treated with caution. The other limitation of this study is that it focused on only four characteristics of the board of directors. The model could be extended to take board processes, accountability and social responsibility into consideration. The other limitation is that it would have been better if this study had a longitudinal perspective. This study is essentially cross-sectional, looking at board characteristics at a particular point in time. Future research could replicate the study in other provinces in order to test the validity and reliability of the scale. Another prospect for future research is to conduct comparative studies of the relationship between board characteristics and corporate performance, for example between non-life insurance companies in a developed and an emerging country.

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