



**Board Composition and Firm Performance: The
Moderating Role of Corporate Governance Practices
Perception in Iraq**

by

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LIST OF ABBREVIATIONS

ISX	Iraqi Stock Exchange
CEO	Chief Executive Officer
KRG	Kurdistan Reign Government
GDP	Gross Domestic Product
BSX	Baghdad Stock Exchange
OECD	Organization for Economic Co-operation and Development
SEC	Securities and Exchange commission
ROA	Return on assets
ROE	Return on equity
CG	Corporate Governance
BODs	Board of Directors
BC	Board Composition
LLC	Limited Liability Companies
JSC	Jordan Securities Commission
NFMPS	non-financial manufacturing performance
BSC	Balanced Scorecard
BE	Board Educational
FP	Firm Performance
NP	Non-firm Performance
AC	Accountability
FA	Fairness
TR	Transparency
IN	Independence

BP	Board Political
BED	Board Ethnic Diversity
FM	Female Member
BGD	Board Gender Diversity
ISIS	Islamic state in Iraq and Sham
ROI	return on investment
PLS	Partial Least Squares
SPSS	Statistical Package for Social Sciences
CMV	Common Method Variance
CMB	Common Method Bias
SEM	Structure Equation Modeling
CR	Composite Reliability
AVE	Average Variance Extracted

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Komposisi Lembaga Pengarah dan Prestasi Syarikat: Peranan Moderator Persepsi Amalan Tadbir Urus Korporat di Iraq

ABSTRAK

Tadbir urus semakin diiktiraf oleh komuniti perniagaan, pihak perundangan dan sekuriti pasaran modal sebagai pemacu asas prestasi korporat. Kajian ini mengkaji kesan komposisi Lembaga Pengarah (pendidikan Lembaga Pengarah, hubungan politik Lembaga Pengarah, kepelbagaian etnik Lembaga Pengarah dan kepelbagaian jantina Lembaga Pengarah) ke atas prestasi syarikat. Selain itu, mengkaji kesan amalan tadbir urus sebagai pembolehubah yang menyederhanakan hubungan antara komposisi Lembaga Pengarah dan prestasi syarikat-syarikat di Iraq. Kajian ini menggunakan Teori Agensi dan Teori Echelon Atasan untuk membangunkan hipotesis. Kaedah kuantitatif (soal selidik) telah dilaksanakan untuk mencapai objektif penyelidikan. Sampel kajian terdiri daripada 207 syarikat di Iraq, termasuk 107 syarikat yang disenaraikan di Bursa Saham Iraq dan 100 syarikat dengan modal yang besar dan tidak disenaraikan di Bursa Saham Iraq. Soal selidik itu digunakan untuk meneroka tadbir urus di Iraq dengan mendapatkan dan menganalisis persepsi pihak pengurusan atasan. Pakej Statistik Sains Sosial (SPSS) dan Pemodelan Persamaan Struktur (SEM) melalui Smart PLS 3.3 telah digunakan untuk menganalisis hipotesis. Kajian ini menyediakan bukti kukuh bahawa pembolehubah komposisi Lembaga Pengarah seperti pendidikan Lembaga Pengarah, hubungan politik Lembaga Pengarah dan kepelbagaian etnik Lembaga Pengarah memberi kesan ketara kepada prestasi syarikat dalam konteks Iraq. Walau bagaimanapun, keputusan kajian mencadangkan pengaruh kepelbagaian jantina Lembaga Pengarah tidak mempunyai hubungan ketara. Selain itu, terdapat bukti bahawa kehadiran amalan tadbir urus cenderung untuk menyederhanakan secara negatif pengaruh hubungan politik lembaga pengarah dan kepelbagaian jantina lembaga pengarah ke atas prestasi syarikat. Sebaliknya, amalan tadbir urus secara positif menyederhanakan hubungan antara kepelbagaian etnik Lembaga Pengarah dan prestasi syarikat. Walau bagaimanapun, tiada hubungan yang signifikan ke atas tahap pendidikan Lembaga Pengarah dan prestasi syarikat. Keputusan ini menekankan beberapa perkara kepada pihak perundangan dan implikasi pengurusan, di antaranya adalah, menyeru usaha yang lebih bersepadu dalam melaksanakan penyelesaian tadbir urus yang baik untuk bukti masa depan pasaran saham di Iraq. Tumpuan kepada Iraq adalah penting kerana ia membolehkan pihak pembuat dasar, pengurus dan penyelidik menyiasat hubungan antara Komposisi Lembaga pengarah dan prestasi yang konsisten dengan menggunakan teori agensi terhadap latar belakang institusi khusus untuk syarikat-syarikat di Iraq. Sumbangan kedua berkaitan penyiasatan empirikal terhadap kesan amalan tadbir urus sebagai pengukuhan terhadap prestasi korporat. Sumbangan ketiga, di Iraq, persekitaran perniagaan dikuasai oleh sektor swasta. Hasil kajian ini menunjukkan bahawa pelaksanaan amalan tadbir urus yang baik meningkatkan prestasi syarikat.

Board Composition and Firm performance: The Moderating Role of Corporate Governance Practices Perception in Iraq

ABSTRACT

Governance is increasingly recognized by the business community, regulators and capital market authorities as a fundamental driver of corporate performance. This study examined the impact of the Board Composition (Board Educational Level, Board Political Connection, Board Ethnic Diversity, and Board Gender Diversity) on firm performance. Then, examine the impact of Corporate Governance Practices perception as a variable that moderate the relationship between the composition of the board of directors and the performance of Iraqi companies. This study used Agency Theory and Upper Echelon Theory in developing the hypotheses. A quantitative research method (questionnaire) has been adopted to achieve research objectives. The study sample consists of 207 Iraqi companies, including 107 companies listed on the Iraqi Stock Exchange and 100 companies with large capital and not listed on the Iraqi stock exchange. The questionnaire was used to explore corporate governance in Iraq by obtaining and analyzing top management perceptions. Statistical Package for the Social Sciences (SPSS) and Structural Equation Modeling (SEM) through Smart PLS 3.3 have been used to analyze the hypotheses. The study provides robust evidence that board composition variables such as board educational level, board political connection and board ethnic diversity significantly affect the Firm Performance in the Iraqi context. However, the result propounds non-significant influences of Board gender diversity. Moreover, there is evidence that the presence of Corporate Governance Practices Perception tends to negatively moderate the influence of board political connection and board gender diversity on corporate performance. On other hand, corporate governance practices positively moderate the relationship between board ethnic diversity and firm performance, while does not affect board educational level on firm performance. These results give rise to certain regulatory and managerial implications, all of which, calls for more concerted efforts in strategically implementing prudent governance solutions in order to the future proof Iraqi market. The focus on Iraq is important because it allows regulators, managers and researchers to investigate the link between the Board Composition and consistent performance using the agency's theory against an institutional background specific to Iraq. The second contribution relates to the empirical investigation of the impact of Corporate Governance Practices Perception as moderate on corporate performance. The third contribution, in Iraq, is dominated by the private sector in the business environment. The results of this study show that the implementation of good governance practices increases the performance of companies.

CHAPTER 1: INTRODUCTION

1.1 Background to the study

The effectiveness of the company board as a fundamental institution in the internal governance of a firm and its effect on company behavior is one of the utmost discussed issues in the literature currently (Soare et al.,2021; Saleh et al.,2021; Safari,2017; Arora & Sharma, 2016). The board of directors' responsibility is to guide and authorize the company's tactical decisions (Chams, & García-Blandón,2019); appoint, supervise and remunerate senior managers and connecting the company to the exterior environments; and provide information to managers (Kılıç & Kuzey, 2016). These roles make the board of directors one of the vital interior company governance control mechanisms in an entity (Hernández-Nicolás,2019). However, these functions and approaches, in turn, influence the company's financial performances and overall capital expenditure (Terjesen, Couto, & Francisco 2016).

Performance, as an essential requirement for the survival and growth of a company, is considered as the process by which the limited number of resources available to an organization are effectively and efficiently managed in achieving its predetermined objectives for both short and long-term periods. It is the increase in wealth of a shareholder from the beginning of one accounting period to the end of another period (Le & Phan,2017; Abdulsamad et al.,2018). In this regard, the any objective of shareholders investing in a venture is to ameliorate their wealth from one level to a better level, and this could only be achieved when the business is doing well. Thus, the performance of a

company will depict how better-off a shareholder has become on the investment in an entity over a given period (Kakanda & Salim,2017).

However, the board similarly has the duty of initiating changes in organizations and facilitating procedures that promote the organization's mission to help improve its performance (Megginson., et al,2019). Further, the boards try to protect the stakeholder's interests in progressively competitive environments while preserving management competence and accountabilities in pursuing good corporate performances (Ballesteros et al.,2017; Gebba, 2015; El-Gammal et al.,2017). A stronger board could show very vital economic roles in company performances. They could offer connection among the company and its environments, securing important resources (Waheed & Malik,2021) as well as playing active roles in a company's tactical decision-making (Osemeke et al.,2020).

In order to be efficient, Boards must take steps to guarantee that insiders and executive owners have no unauthorised control of the operations and choices of the Board, as well as in their nomination process (CFA Institute, 2020). Because boards are supposed to be independent of shareholders in order to offer a diverse array of views on strategy, governance, and financial performance, boards should be required to maintain sufficient independence to provide shareholders and other interested parties with differing views on strategy, governance, and financial performance. Boards should do so by seeking competent professionals and abstaining from nominating individuals with a high number of previous board memberships (CFA Institute, 2020). A corporate board of directors' primary responsibility is to safeguard shareholders' assets and to ensure they receive a positive return on their investment (Naimah, 2017). The board of directors is

the highest governing authority within the management structure of a corporation or publicly traded business. It is the board's job to select, evaluate, and approve compensation for the company's chief executive officer (CEO), evaluate the attractiveness of and pay a dividend, recommend stock splits, oversee share repurchase, approve the company's financial statements, and recommend or reject merger and acquisition opportunities, and the like (CFA Institute, 2020).

Additional issues include board appointments for women, and multiple-year terms for board members. There is no clear consensus regarding the relationship between gender diversity on boards of directors and firm performance. Several studies have established that increasing female representation on the board of directors improves the firm's performance. Adams (2016) and Saleh et al.:2018a, as well as Marinova, Plantenga, and Remery, 2015.

In Iraq for instance, women are restricted to participate in education and the labor force due to reinforced conservative gender roles in the country (Dodge, et al., 2018). This indicates the marginalization of women in terms of the role they can play as a member of the board of directors in Iraq companies. In the same vein, Carter et al. (2003) argued that although very varied boards might be more an activist one, there is no assurance that monitoring is very efficient as various board members might be marginalized. Because of these costs and benefits consideration, the business cases for gender variety appears less obvious cuts and depend on a particular circumstance. This unlocks the floors for additional empirical focused research on the association between gender diversities and company performances (Marinova, Plantenga & Remery, 2016).

Another important factor is the board's diversity, which includes aspects such as gender, age, nationality, ethnicity, and education level (Ballesteros et al.2017). Many academics were interested in how the board of directors' level of education influences firm performance. Additionally, the educated board is believed to be innovative, thus making things convenient for corporate development in all aspects (Zhong, 2016). Previous studies demonstrated that boards with diverse gender, ethnicity, and cultural backgrounds could lead to more socially conscious behaviour (Ballesteros et al.2017; Ntim,2015).

However, Iraq is among the most religiously and ethnically diverse countries in the world. This includes Christians, Kurds, Turkmens, Assyrians, and Yezidi ethnicities in Iraq. The overwhelming majority of Muslims are Shi'a Arabs, Sunni Arabs, and Kurds, all of whom are Muslims. About 10% of the population are ethnic Shabaks, Turkmens, Faili Kurds, Palestinians, Roma, Christians, Sabian-Mandaenans, Yezidis, and Baha'i, with Shi'a and Sunni Muslims making up the majority (Cerami, 2018). Iraqi minority rights are now in severe straits on all levels: political, civic, and cultural. Iraq's ethnic and religious minority, along with other susceptible populations, are still exposed to violence, religion discrimination, segregation, and loss of property rights (Cerami, 2018).

Furthermore, Wang & Hooy (2018) has emphasized the importance of the political connection of board members as one of the significant aspects of firm Board Composition. Brogaard et al. (2015), argued that the presence of political power in the firm assist its officers and directors to obtain an influence on law and regulations and grant them accesses to exclusive information, that allows them to anticipate economic variations and decrease uncertainties. Nevertheless, the entrance into the business world

permits politicians to collect financial supports in the time of the election, fundamentally in the form of donation (Brogaard et al. 2015).

Prior study proclaimed that having good friends in government is valuable social capital for businessmen (Ling et al., 2016). On the other hand, World Bank Report (2018) stated that corruptions, as well as poor governance, are still a crucial issue in Iraq. The country is obstinately classified in between or under the tenth percentile worldwide according to the indicator of government' efficiency, rules of law, as well as controls of corruption. Iraq's performance was mainly poor in the indicator for constancy and lack of violence, rules of law, and controls of corruption. This has resulted in lower firm performance especially for less politically connected firms since priority is always given to those companies with strong political connections with the government (World Bank Report, 2018).

According to Upper-echelon theory, a company's performance is significantly impacted by the demographic factors (Board Educational Level, Board Ethnic Diversity, Board Gender Diversity) of its board of director members or top management, as well as its decision-makers. In view of the fact that education is a demographic characteristic of the board, it should be mentioned that education is on the board's agenda (Jung and Ejerme 2014).

The agency theory suggests that information asymmetry causes principal-agent conflict (Ballesteros et al.,2017; Ciftci et al.,2019) Corporate Governance (CG) was also required for the process of monitoring managers' accountability, decisions, and forecasts in order to reduce agency problems and conflict of interest. Consequently, risk disclosure

can help alleviate agency conflicts and enable shareholders to build a relationship of trust with managers (Kakanda & Salim,2017; Haj et al.,2020). As a result, boards and corporate governance are thought to influence company performance. It's also worth investigating their effect on firm performance.

The framework of corporate governance practices issued by the Organization for Economic Cooperation and Development (OECD) includes several components that usually point out to the level of corporate governance in the company. Whereas the duty of management, the board of directors, and the audit committee towards investors and all other stakeholders is to work on harmonizing these components and arranging priorities in order to reach the required level of governance (El-Gammal et al.,2017).

Prior studies have investigated the direct link between CG and long-term firm performance (Haj et al.,2020; Bhagat & Bolton, 2019; Duppati et al. 2019). However, the results still are inconclusive and differ within the context. Furthermore, although CSR has attracted a number of researchers to examine its determinants, research on the consequences of this type of disclosure is still limited and particularly scarce in developing countries.

Improving corporate governance practice is important as shareholders are more concerned about the return on the money invested in the company as the supplier of capital. Shareholders, as well as regulators, highlight the importance of effective corporate governance mechanisms. Effective corporate governance is critical in ensuring and increasing investors' confidence. Effective corporate governance enhances firm performance and protects shareholders interest (Talab, H. R, et all, 2017)

In addition, Corporate Governance Practices Perception have been a concerning issue by many Asian countries after the Asian Financial Crisis in 1997 including Iraq (Zabri, Ahmad & Wah, 2016). So, does propose good corporate governance practices in Iraq may influence the performance of Board Composition and firm performance will be the main objective of this study.

Although, there were numerous studies conducted on the relationship between firm performance and Corporate Governance, the problem still exists especially in Iraq (Gedi, F. F., & Nayan, S. 2018). The reason for the lack of studies that dealt with corporate governance in Iraq is due to the absence of an Iraqi law requiring Iraqi companies listed on the stock market to follow the corporate governance guide. Therefore, this study attempts to examine the moderating role of Corporate Governance Practices Perception on the relationship between Board Composition represented by (board educational level, political connection, board ethnic diversity and female membership on board), and the performance of firms in Iraq.

1.2 Problem Statement

Corporate governance has for long become an issue of global concern due to excessive corporate failures that resulted from poor corporate governance practice. Among the cases are Enron, World Com and Lehman Brothers in the United States, Parmalat in Italy, and Malaysian Airlines System (MAS) in Malaysia, Spring Bank Plc, and Fin Bank Plc in Nigeria (Nugroho,2021; Shahwan, 2015). The central theme of the issue being debated is the failure of the board of directors in playing their role of monitoring and counselling and reporting the activities of the company for the interest of

shareholders, whose expectations are having a better return on their investments (El-Gammal et al.,2017). Also, the issues of corporate failures as well as its association with poor governance which result to weak performances is similarly seen in Iraq (Shahwan,2015). Regarding this, the Iraq stock exchange was shocked from the worldwide economic disasters which resulted to loss of works and investors assurance in the capital markets, alongside, doubts in the efficiency of current Corporate Governance Practices Perception (Ironkwe & Adee, 2014).

As shown in Figure 1.1, the performance of Iraq listed firms is discouraging given the deteriorating nature of its price index performance between 2015 through 2019. Therefore, the issue of control of listed firms is subject of public interest where the government is making concerted efforts to remove administrative and financial corruption which has penetrated into the Iraqi economy (Al-Maryani, 2015). Previous studies have opined that the reason for such poor performance can be specifically traced to the fall in the confidence level of the investors due to ineffective Corporate Governance (CG) in Iraq (Gedi, F. F., & Nayan, S. 2018). Consequently, many investors have transferred their hard-earned income and invest it in safer economic and business environment.



Figure 1-1 :price index performance in Iraq
Source: ISX market (2020)

As can be seen from above figure, the index of the share prices traded on the Iraqi stock Exchange where the higher price recorded in 2015 where they recorded 730.56 points, but prices began to decline in 2016, 2017, 2018 and 2019, where the lowest prices were recorded in 2019, where they recorded 493.76.

Although, there were numerous studies conducted on the relationship between firm performance and Corporate Governance, but the problem still exists especially in Iraq (Gedi, F. F., & Nayan, S. 2018). Even though some of the variables have been discussed by past scholars, the majority of the literature emanated from developed nations and of which their results may not be generalizable to the Middle East countries in general and Iraq in particular, because of differences in an organization setting, cultural affiliation, and geography (Gedi, F. F., & Nayan, S. 2018).