

## Prithvi Journal of Research and Innovation

[A Peer-Reviewed, Open Access Multidisciplinary Bilingual Journal; Indexed in NepJOL]

ISSN 2705-4888 [Print]; ISSN 2705-4896 [Online]; JPPS Star-Rated Journal

Volume 5; 15 December 2023; pp. 85-101

eJournal Site: <http://ejournals.pncampus.edu.np/ejournals/pjri/>

# From Corporate Board to Balance Sheet: Board Characteristics and Financial Performance of Commercial Banks in Nepal

**Resham Raj Sharma**

Faculty of Management, Prithvi Narayan Campus, Pokhara, Nepal

ORCID: <https://orcid.org/0009-0008-1611-2521>

### Article History:

Submitted 01 October 2023

Reviewed 19 November 2023

Revised 23 November 2023

Accepted 02 December 2023

### Corresponding Author:

Resham Raj Sharma

Email: [reshamsharma33@gmail.com](mailto:reshamsharma33@gmail.com)

### Article DOI:

<https://doi.org/10.3126/pjri.v5i1.60694>

### Copyright Information:

Copyright 2023 © Authors of this journal; With authors' permission, the copyright is transferred to the publisher for the first edition only. This work is licensed under a [Creative Commons Attribution-NonCommercial 4.0 International License](https://creativecommons.org/licenses/by-nc/4.0/).



### Publisher:

Centre for Research and Innovation

Prithvi Narayan Campus

Tribhuvan University, Pokhara, Nepal

[Accredited by UGC, Nepal]

Tel.: +977-61-576837

Email: [research@pncampus.edu.np](mailto:research@pncampus.edu.np)

URL: [www.pncampus.edu.np](http://www.pncampus.edu.np)

### ABSTRACT

This study aims to examine the impact of board characteristics on the financial performance of commercial banks in Nepal. The study utilized census sampling of all commercial banks having shares listed and actively traded in the secondary market, NEPSE. Descriptive and inferential tools were employed including multiple linear regression models to analyze the impact of board characteristics on financial performance based on the longitudinal data of 21 commercial banks collected from the secondary sources over the period of ten years from 2013 to 2022. The study shows that strictly followed mandatory requirements regarding board size, board independence, and board committees after the enforcement of BAFIA in 2017 along with a relatively small representation of women and independent directors in the boardroom during the study period. The findings show a statistically significant negative impact of board diversity and board committees along with an insignificant impact of board size and board independence on ROA and ROE. The findings of the study also indicate that a higher proportion of women directors and a large number of board committees in the board have contributed

negatively to the financial performance of commercial banks in Nepal. However, the comprehensive outcome of this research challenges the agency theory and points towards the presence of tokenism in the inclusion of women and independent directors. The

results of the descriptive analysis assimilate to the agency and stakeholder theory respectively by ROE and ROA. The findings of this study have practical implications for banking regulators, legislators, and banks in policy formulation relating to board characteristics.

**KEYWORDS:** Board characteristics, board independence, commercial banks, corporate governance, financial performance

## INTRODUCTION

Corporate governance has been a significant topic in the business world for the last few decades. It has garnered attention from boardrooms, the media, and various stakeholders (Subramanian, 2015). Issues related to financial crises, economic downturns, corporate frauds, and failures have encouraged discussions, debates, and empirical works about corporate governance in both developed and developing economies around the world (Brown & Caylor, 2006). Sound corporate governance mechanisms play a crucial role in drawing foreign direct investments and portfolio capital by encompassing both strict legal regulations and flexible industry standards. A commonly held belief is that firms possessing a strong corporate governance framework contribute to superior financial performance and stability (Arnwine, 2002). Thus, these mechanisms not only foster the expansion of financial markets but also promote the broader economic advancement of the economy through better firm performance.

Over the past two decades, the South Asia Region has witnessed significant advancements in enhancing its national regulatory frameworks and establishing effective corporate governance systems. The notable developments regarding the corporate governance system have been instigated by both international initiatives like the Organization for Economic Co-operation and Development (OECD) and national government bodies including the private sectors in this region. These initiatives include the Asian Roundtable on Corporate Governance and the 2003 white paper on corporate governance in Asia from OECD which outlined an ambitious reform agenda. Additionally, the World Bank has been actively monitoring the adherence to international corporate governance standards. This progress has also been shaped by the involvement of international financial institutions collaborating under the guidance of the International Finance Corporation (Kirchmaier & Gerner-Beuerle, 2021).

Corporate governance becomes pivotal in reducing the transaction costs and the actual costs associated with capital, which is a fundamental pillar in economic development and financial stability. Corporate governance failures can have significant adverse effects on the stock markets, sentiments, and confidence of investors, and result in broader economic impacts and even some social implications. However, the central aspect of this governance issue revolves around the characteristics of corporate boards, notably how they are composed, their size, diversity, independence, board committee formation and functioning, and how often they meet (Jan & Sangmi, 2016). Thus, the attributes of the corporate boards are considered a pivotal component in the corporate governance mechanism that holds significant influence over the operations and performance of firms, including banks and financial institutions.

The reforms in corporate governance hold immense importance for developing markets like Nepal, which are diligently striving to attract Foreign Direct Investment and stimulate increased capital market savings (GC, 2019). As financial liberalization and

reforms become more prevalent and there is a growing trend of public companies being listed on the Nepali stock exchange, there is a pressing need for improved corporate standards and governance mechanisms. The corporate governance failures in the financial institutions i.e., Nepal Development Bank, Nepal Share Market Finance, Samjhana Finance, Capital Merchant Banking and Finance Limited, and Gorkha Development Banks in Nepal over the last 15 years have sparked substantial interest among policymakers and regulators in the advancement of corporate governance practices. Consequently, Nepal Rastra Bank, the Securities Exchange Board of Nepal, and the Nepal Stock Exchange have made efforts through regulatory provisions for robust corporate governance mechanisms in Nepal.

Nepal, a country characterized by a rich cultural heritage and diverse socio-economic structures, has experienced transformative changes in its banking sector over recent decades. The regulatory environment, governed by the Nepal Rastra Bank (NRB), has witnessed notable shifts aimed at modernizing banking practices while maintaining stability within the financial system. Moreover, the socio-economic landscape, marked by varying regional demographics and economic disparities, significantly influences banking operations and governance practices. Cultural norms and traditions also hold considerable influence over corporate practices in Nepal, affecting decision-making processes and board dynamics within commercial banks. The interaction between values centered on collectivism, hierarchies, and social relationships aligns with board characteristics, potentially shaping a distinct cultural landscape relevant to the governance mechanisms and financial performance of Nepali banking institutions.

The Nepali commercial banking sector, consisting of government, domestic, and joint venture banks, plays a crucial role in the overall economy. According to the Economic Survey of 2022, the banking sector accounts for a substantial 87.2 percent share, with commercial banks alone contributing 58.9 percent to the assets and liabilities structure of Nepal's financial system. In an increasingly intricate and competitive global financial landscape, the significance of corporate governance, particularly the influence of board characteristics, cannot be overstated when it comes to shaping the performance and resilience of Nepali commercial banks. The boardroom, as the apex authority of making strategic decisions within an organization, becomes a critical factor for directing operations and determining the financial performance and financial stability of the banks. Nepali commercial banks, in their pursuit of sustainable growth and stability, navigate this complex relationship between the dynamics of their boardrooms and the reflections of these dynamics on their balance sheets. This research is particularly relevant in the case of Nepal to understand the status of board characteristics and financial performance and how they affect the financial performance of banks. Thus, this paper aims to explore the interplay between the boardroom and balance sheet with a special focus on unveiling the impact of board characteristics on the financial performance of Nepali commercial banks. This research endeavors to explore relationships, shedding light on the mechanisms that connect the boardroom to the balance sheet in the unique context of Nepali commercial banks using the rational ground of agency theory, resource dependence theory, and stakeholder theory.

This study explores the bearing of board characteristics on the financial performance of Nepali commercial banks by considering the four key attributes of the board namely board size, board independence, board diversity, and board committees. It

utilizes accounting-based measures of financial performance like return on assets (ROA) and return on equity (ROE) as performance indicators. The multiple linear regression models are employed with different tests for the reliability and validity of the models. This study contributes significantly to the area of corporate governance literature in two ways. First of all, it extends the existing literature by focusing on the board characteristics and their impact on the financial performance of commercial banks from the developing market. Most of the prior studies in the area of corporate governance and board characteristics were focused on developed economies. Second, this study sets it apart from the other studies in terms of the theoretical ground this study relies on and the sample size it considers.

The remainder of this paper is structured as given under. The second section presents a review of the literature, while the section third describes the sample, data, and methodology, section four reports empirical results and finally, section five includes conclusions.

### **LITERATURE REVIEW**

Scholars from around the world, having interest and expertise in a variety of disciplines, such as finance, economics, laws, strategic management, and organizational behavior have extensively examined the impact of boardroom activities on firm performance on the grounds of different theoretical perspectives. Notable studies in corporate governance and board attributes (Berle & Means, 1932; Fama, 1980; Jensen & Murphy, 1990) have predominantly based on agency theory and emphasized the critical role of corporate board and boardroom activities for effective monitoring in a firm and better financial performance.

Pfeffer and Salancik (1978); Daily et al. (2003); Hillman and Dalziel (2003) have based their studies on the resource dependence theory. Recognizing the need for a comprehensive approach, Hillman and Dalziel (2003) proposed a blending of agency theory with resource dependency theory to understand the complex nature of principal-agent relationship and corporate governance including the studies relating to board characteristics and firm performance. Similarly, Freeman (1984) highlighted the constraint of agency theory and suggested the multiple agency theory (MAT) for studies relating to board characteristics, corporate governance, and firm performance as an alternative. Aguilera et al. (2015) stated that the base of multiple agency theory and the blending of theories build a strong theoretical foundation for scholarly works on board characteristics and financial performance.

Agency theory stresses the crucial role played by the corporate board in mitigating agency conflicts and agency-related costs, which results in good governance and better firm performance. In contrast, resource dependency theory highlights the role of the corporate board to link with a firm's external resources, financial performance, and stability. Notably, stakeholder theory advocates board composition plays a critical role in guiding the company towards more ethical and sustainable business practices, leading to enhanced financial performance by considering the interests of divergent stakeholders. These theories converge on the board's significance in influencing firm performance, but they diverge in their emphasis on mechanisms such as conflict resolution, resource leveraging, ethical considerations, and governance. On the ground of this rationale, the present study incorporates multiple theories i.e., agency theory and resource dependency

theory by following Hillman and Dalziel (2003) along with the stakeholders' theory to investigate the relationship between board characteristics and financial performance of Nepali commercial banks.

### ***Board Characteristics and Financial Performance***

Board characteristics include the traits, attributes, and behaviors of the individuals who serve on a board of directors in the boardroom of a firm. Fama (1980) has defined board characteristics as the proportions of the boardroom of a corporation, including the size, the number of independent directors, diversity in the board, the number of committees and size, experiences of the members, and the flow of information within the boardroom and from board member to the managers and outsiders. Abu et al. (2016) have detailed the board characteristics as board autonomy, gender diversity in the boardroom, the board size, nationality and ethnicity of members, education and experiences, board committees, the duality of CEO, and a number of board meetings. Research has shown that board characteristics can have a significant impact on the performance and effectiveness of the board through enhanced good governance, decision dynamics, and ethical practices in the organizations (Abu et al., 2016; Cheng, 2008). Board characteristics play a pivotal role in shaping firm performance.

The evidence of the past literature shows that corporate scandals burned over the past few decades were connected to corporate governance and the board characteristics in this or that way. Orozco et al. (2018) argued that the board and its characteristics are the important elements contributing to corporate governance and thus firm performance and stability. Thus, the basic conceptualization of this paper is that the financial performance of Nepali commercial banks depends on the board characteristics. A large number of researchers such as Yermack (1996); Jackling and Johl (2009); Darmadi (2011); Terjesen et al. (2015); Mishra and Kapali (2018); G.C. (2019); Gadtaula et al. (2021); Arvanitis et al. (2022) have made scholarly attempts on the issue of board characteristics and financial performance in the different time frame and context and revealed consistent link between board characteristics and firm performance.

### ***Financial Performance and Metrics***

Financial performance is an economic achievement of producing superior sales, profitability, and value to its shareholders. Financial performance refers to a company's ability to generate profits and manage its financial resources effectively and is reported in terms of profitability, resource expansion, sales growth, value, and so forth (Brigham & Ehrhardt, 2016). Ross et al. (2008) explained financial performance as the degree to which a firm's financial health is reflected in terms of operating results over a period. Therefore, financial performance is a key indicator of a company's overall health and ability to succeed in the marketplace. Firms with high levels of financial performance are more likely to satisfy the divergent interests of their stakeholders, engage in proactive risk management practices, and tend to have a greater focus on innovation and sustainable business.

The financial performance of a firm is measured in a variety of ways. The existing literature on financial management and accounting has identified various measures of firm financial performance, which can be classified into accounting-based measures and market-based measures (Khatab et al., 2011). The accounting-based

measures include return on assets, return on equity, net profit margin, net interest margin, earning per share, return on sales, growth on sales, labor productivity, operating profit, cost of capital, sales to assets, etc. Similarly, the market-based measures include Tobin's Q, market-to-book value, price-earnings ratio, dividend yield, market value added, etc.

### ***Board Size and Financial Performance***

Board size refers to the number of members in the committee of the Board of Directors and holds a central place in determining the effectiveness of the committee of the Board of Directors. The empirical evidence shows the lack of a common consensus in regard to the effect of the board size on the effectiveness of the board of directors and financial performance. Empirical works by Lipton and Lorsch (1992); Yermack (1996); Rashid et al. (2010); Orozco et al. (2018) reported a negative relationship between board size and firm performance and argued that the large board size will result in higher communication, coordination, and management costs along with the cost of slow decision-making and thus the board size is connected negatively with financial performance. Contrary to this, scholars like Coles et al. (2008); Gadtaula et al. (2021); Hamid and Purbawangsa (2022) reported that board size is positively correlated with firm performance, a large board size results in effective decision-making for guiding organizational activities to the accomplishment of goals.

### ***Board Independence and Financial Performance***

Board independence denotes the number of independent and professional directors in the boardroom. Fama (1980) argues that the independent judgment of the directors is important for reducing agency-related issues, problems, and costs. The board independence is supposed to be higher when the number of independent and non-executive directors increase in the boardroom. Fama and Jensen (1983) stressed that the presence of the non-executive director on the board is significant as they can monitor and control organizational activities in the best interest of the stakeholders. Sobhan (2021) reported a positive association of board independence and firm performance. Scholars like Arora and Sharma (2016); Haldar et al. (2018); Nepal and Deb (2022) on the other, found a significant negative relationship between board independence and financial performance and stated that independent directors lack practical business knowledge and behavioral considerations, which influenced firm performance and value adversely.

### ***Board Diversity and Financial Performance***

Board diversity indicates the tangible and intangible attributes of the board directors. Tangible diversity consists of the gender, age, and ethnic groups of the members, and the experiences, education, skills, and other personal qualities of the directors are included in the intangible diversity Fama (1980). However, diversity shapes the ways people perceive, behave, and interact with others in a group, which is important in the boardroom. A large number of studies relating to the impact of board diversity on firm performance and value exist in the literature on governance. Carter et al. (2010); Terjesen et al. (2015); Kathuria and Dash (2016); Acharya (2018); Arvanitis et al. (2022) reported the positive impact of board diversity on the firm performance. Opposing to these results, Darmadi (2011); Arora and Sharma (2016); Mishra and Kapali (2018);

Nepal and Deb (2022) have reported the negative impact of board diversity on firm performance.

### ***Board Committees and Financial Performance***

Board committees refer to the board-level committees led by members of the board of directors in a company. Board committees permit an improved allocation of resources, skills, roles, and responsibilities among the smaller group of directors and increase the time and devotion of the directors in the key area of his / her expertise which enhances a strong governance mechanism (Carter et al., 2010). The practice of such board committees enhances transparency, governance mechanisms, and firm performance through the use of specialization and specification in the boardroom (García-Ramos and García-Olalla, 2011). Empirical works relating to the roles and impact of board committees on firm performance and value were found to be inconclusive. A large number of studies relating to board committees and financial performance reported the positive impact of board committees on firm performance (Carter et al., 2010; García-Ramos et al., 2011; Gafoor et al., 2018; Alodat et al., 2021). In contrast, the studies by Al-Matari et al. (2012); Pucheta-Martínez and Gallego-Álvarez (2020) reported a negative impact of board committees on the market-based measure of firm performance i.e., Tobin's Q.

## **METHODOLOGY**

### ***Sample and Data***

The population unit was defined as the total number of class 'A' commercial banks in operation as on January 14, 2023, and listed in the Nepal Stock Exchange (NEPSE) for active stock trading in the secondary market. At that specific date, there were 22 class 'A' commercial banks in operation, with 21 of them having stocks actively traded in NEPSE. Rastriya Banijaya Bank, despite being a class 'A' commercial bank in operation on the stated date, was excluded from the population due to its stocks not being available for trading in NEPSE. Thus, the population and sample for the study have been 21 class 'A' commercial banks. On this ground, the study employed a census sampling technique in which the entire population was taken as a sample. The major justification of the census study is that it provides more accurate and comprehensive information, it also provides accurate estimates of population characteristics, such as mean and proportions (Trochim, 2005).

The variables utilized to measure the constructs, board characteristics, and financial performance are quantitative and thus the study is based on quantitative data. The required data have been collected using secondary sources. Data regarding board size, board diversity, board independence, board committees, and assets size along with the data required to compute return on equity (ROE) and return on assets (ROA) were obtained from the annual report published on the respective websites of banks under study. Likewise, the data relating to bank type, and information relating to directives were collected from the report published by Nepal Rastra Bank. Green (1991) has suggested for enough observation, a minimum of  $50 + 8k$ , where  $k$  stands for the number of predictors in the model, to obtain a reliable regression model with the test of the significance of the overall model and individual predictors. Thus, the study has used data

on board characteristics and financial performance of the sampled banks covering a period from 2013 to 2022.

**Table 1**

*Description of Variables*

Indicators	Variable name	Operational definition
Financial Performance (Dependent) Variable		
ROA	Return on assets	Net income divided by book value of total assets
ROE	Return on equity	Net income divided by book value of equity
Board Characteristics (Independent) Variables		
B size.	Board size	Total number of directors on the board
B ind.	Board independence	Percentage of independent directors on the board
B div.	Board diversity	Percentage of female directors on the board
B com.	Board committees	The total number of board-level committees
Control Variables		
A size.	Bank asset size	The natural log of book value total assets
B age.	Bank age	Number of years the bank has been established

*Description of Variables*

The variables used in this study are classified into three main categories, dependent variables, independent variables, and control variables. The study has used the techniques for the measurement of variables as adopted by Eisenberg et al. (1998); Gafoor et al. (2018); G.C. (2019); Habtoor (2022). Independent variables include board size (B size.), board independence (B ind.), board diversity (B div.), and board committees (B com.). The independent variable board size, board independence, board diversity, and board committees are measured using the total number of board members, percentage of independent directors, percentage of female directors on the board, and the number of board-level committees and sub-committees led by board members respectively. The dependent variables consist of an accounting-based measure of financial performance i.e., return on asset (ROA) and return on equity (ROE). Finally, the control variables used to control the possible impact on financial performance are bank asset size (A size.) and bank age (B age.). The description of variables is presented in Table 1.

*Econometric Models*

Descriptive and inferential statistics have been employed in the study. To assess the board characteristics and financial performance, descriptive statistics namely mean, standard deviation, minimum, and maximum are employed in the study. Inferential statistics i.e., correlation and multiple linear regression models are used to examine the effect of board characteristics on the financial performance of commercial banks in Nepal. This study has used a tested model following (Carter et al., 2010; García-Ramos et al., 2011; Gafoor et al., 2018) in assessing the impact of board characteristics on the financial performance of Nepali commercial banks using the data collected from 21 banks covering the period of 10 years from 2013 to 2022.

$$ROA_{it} = \beta_0 + \beta_1 B \text{ size}_{.it} + \beta_2 B \text{ ind}_{.it} + \beta_3 B \text{ div}_{.it} + \beta_4 B \text{ com}_{.it} + \gamma \text{ Control Variables} + \varepsilon_{it}$$

$$ROE_{it} = \beta_0 + \beta_1 B \text{ size}_{.it} + \beta_2 B \text{ ind}_{.it} + \beta_3 B \text{ div}_{.it} + \beta_4 B \text{ com}_{.it} + \gamma \text{ Control Variables} + \varepsilon_{it}$$



Where  $i$  and  $t$  represent the bank and periods respectively.  $\beta_0$  is the intercept,  $\beta_1$  to  $\beta_4$  are the beta coefficients of the regression model,  $\gamma$  is the coefficients associated with the control variables, and  $\varepsilon_{it}$  = random component.

## RESULTS

### Results of Descriptive Analysis

Table 2 depicts the descriptive statistics for the board characteristics variables, financial performance variables, and control variables considered in the study along with the total number of observations. The mean ROA for the sample over the study period is 1.5 percent with the minimum, maximum value, and standard deviation of 0.5 percent, 3 percent, and 0.5 percent respectively. The average ROA of Nepali commercial banks is higher than the average ROA of both the Chinese and Indian banking sectors as reported by Gafoor et al. (2018). The average ROE is 14.5 percent with the minimum, maximum value, and standard deviation of 4.9 percent, 29.3 percent, and 5.1 percent respectively. However, the mean values of both ROA and ROE observed over the study period are almost similar to the average ROA and ROE of the Nepali banking sector reported by the Financial Stability Report 2022 published by NRB.

**Table 2**

*Descriptive Statistics for Variables of Interest*

Variables	N	Min	Max	Mean	SD
B size.	210	5	10	6.87	1.173
B ind.	210	0	0.2	0.124	0.06
B div.	210	0	0.333	0.083	0.096
B com.	210	1	5	3.28	0.865
ROA	210	0.005	0.03	0.015	0.005
ROE	210	0.049	0.293	0.145	0.051
A size.	210	23.626	26.763	25.273	0.665
B age.	210	3	63	22.36	12.848

The mean value of the board size of 6.87 with the minimum and maximum values of 5 and 10 directors respectively. This result indicates that the board size of all the commercial banks during the study period is around seven, the optimum board size recommended by the BAFIA 2017 including the minimum and maximum number of directors. The mean value of B ind. of 12.4 percent along with the minimum value of 0 and the maximum value of 20 percent. Prior to the regulatory implementation of BAFIA 2017, the majority of commercial banks had neglected the appointment of independent directors in the boardroom, leading to a minimum value of B ind. set at 0 but following the compulsory provision introduced by BAFIA 2017, all commercial banks have since included independent directors in their boardroom. This result signifies that almost all commercial banks have appointed one independent director as a part to oversee the company, promote professional practices in the boardroom, and protect the interests of all stakeholders.

The mean value for board diversity, scaled using women's representation on the board is 8.33 percent. Nepal Company Act has made a provision to include at least one female director on the board. However, the BAFIA, 2017 has not made such a mandatory provision in the case of financial institutions in Nepal. The increased issue and awareness of social inclusion and gender representation in corporate affairs in Nepal, it is

desired to be a higher representation of female directors in the boardrooms of banking firms. The result regarding women representation is too small compared to the practices of most South Asian countries and that the argument of Kenter (1987).

Nepal Rastra Bank has set out four committees to be represented by the board of directors. Table 2 reveals that the average number of board committees is 3.28, falling below the minimum number of board-level committees prescribed by Nepal Rastra Bank to the Nepali commercial banks. This average is lower than four due to the absence of a compulsory policy before the enactment of BAFIA 2017. However, after the mandatory provision of BAFIA 2017, all commercial banks have adhered to this requirement.

The control variables used in the study were asset size and age of banks. These variables were chosen as the control variables to account for the variations in asset size and age among the banks being analyzed. The bank asset size ranged from 23.626 to 26.736, with a mean value of 25.273. Similarly, the bank age ranged from 3 to 63 years, with a mean age of 22.36 years. The differences noticed in the asset size and bank age could potentially influence the financial performance of the sample through economies of scale and higher earning capacity of assets in operations including established image, goodwill, and bank brand loyalty.

### ***Relationship between Board Characteristics and Financial Performance***

Table 3 presents the results regarding the correlation between the variables of primary interest including control variables. The results exhibit that two key variables of interest namely board diversity and board committees significantly correlated with both ROA and ROE. There is a significant negative correlation of B div. and B com. with ROA, along with a significant negative correlation of B div. and B com. with ROE. It indicates the statistically significant negative relationship between predictors i.e., B div. and B com., and financial performance indicators i.e., ROA and ROE of banks.

**Table 3**

*Correlation between Board Characteristics and Financial Performance Variables*

Variables	ROA	ROE
ROE		1
ROA	1	
B size.	.017	.122
B ind.	-.01	-.133
B div.	-.169*	-.351**
B com.	-.233**	-.358**
A size.	-.001	-.151*
B age.	.316**	.108

\*significant at .05, \*\*significant at .01

### ***Impact of Board Characteristics on Financial Performance***

The impact of board characteristics on financial performance is assessed using multiple linear regression analysis (MLRA). Various test measures have been used to ensure the reliability and validity of the measurement, instruments, and data. First, the normality of the data was assessed using a histogram and outlying observations were identified using Z-Score. No outlying observations were detected for the variables of

primary interest but one outlying observation was detected for the control variable i.e., bank age, which cannot cause serious problems in the regression modeling. Regression diagnostic for assumptions, outlying observations, and influential observations along with the test of multicollinearity was performed using the histogram, normal PP plot of residuals, and scatter plot of residual along with Studentized deleted residuals, central leverage value, Cook's Distance and variable inflation factors (VIF). The test results reported no serious violation of the assumptions of normality, homoscedasticity, outlying observations, influential observations, and severe problems of multicollinearity.

Table 4 presents the results of the regression analysis performed to examine the impact of board characteristics on ROA. It exhibits the negative impact of B ind., B div., and B com. on the ROA with statistically significant results only for two predictors namely B div. and B com. These results are consistent with the results reported by Darmadi (2011); Al-Matari et al. (2012); Nepal and Deb (2022). The R-square of the model is 0.209 which means around 21 percent of the total variation in ROA is explained by the predictor variables under investigation by controlling the effect of asset size and bank age. The fitted model is highly significant ( $F(6, 203) = 8.929, p\text{-value} < .001$ ).

**Table 4**  
*Regression Results for ROA*

Variables	Unstandardized $\beta$	Standardized $\beta$	t	P	VIF
Constant	0.018		1.062	.29	
B size.	0.0001	0.027	0.397	.692	1.218
B ind.	-0.001	-0.004	-0.054	.957	1.174
B div.	-0.011	-0.205	-2.973	.00***	1.225
B com.	-0.002	-0.255	-3.386	.00***	1.452
A size.	0.001	0.005	0.058	.954	2.007
B age.	0.001	0.364	5.007	.000	1.357

$R^2 = .209$

$F(6,203) = 8.929***$

\* $p < .05$ , \*\* $p < .01$ , \*\*\* $p < .001$

The unstandardized  $\beta$  coefficients of B div. and B com. are statistically significant ( $p < .001$  and  $p < .001$ ) for each predictor implying the two predictors have a significant negative effect on ROA. It reveals that the higher percentage representation of women on the board leads to a decrease in ROA. Likewise, if the number of board committee increase, the ROA also decreases, and vice versa. The results depict that the earnings measured in relation to assets react negatively when there is a higher percentage of women representation and a higher number of board-level committees. The results of the standardized  $\beta$  coefficients indicate that out of the two significant variables i.e., B com. and B div., the magnitude of the impact of B com. is higher on the ROA compared to B div. Similarly, B size. and B ind. do not have a statistically significant role to play in increasing or decreasing the ROA. The VIF values, less than five, of all the predictors indicate no serious problem of multicollinearity in the model.

Table 5 presents the results of the regression results for return on equity (ROE). The result shows that the negative impact of B size., B ind., B div., and B com. on financial performance scaled using ROE with statistically significant results for B div. and B com. These results are consistent with the output presented in the correlation

analysis and the findings of Terjesen et al. (2015); Kathuria and Dash (2016); Haldar et al. (2018); Nepal and Deb (2022) regarding the impact of board diversity and board committees on ROE.

The R-square of the model of 0.267 indicating around 27 percent of the total variation of ROE is explained by the four predictors with the control effect of two control variables. The fitted model is highly significant ( $F(6, 203) = 12.321, p < .001$ ). The unstandardized  $\beta$  coefficients of B div. and B com. are statistically significant ( $p < .001$  and  $p < .001$ ) for each predictor implying the two predictors have a significant negative effect on ROE. It reveals that the higher percentage representation of female directors and the large number of board-level committees on the board leads to a decrease in ROE.

**Table 5**  
*Regression Results for ROE*

Variables	Unstandardized $\beta$	Standardized $\beta$	t	p	VIF
Constant	0.12		0.752	.453	
B size.	-0.001	-0.015	-0.23	.818	1.218
B ind.	-0.039	-0.046	-0.702	.484	1.174
B div.	-0.183	-0.344	-5.166	.00***	1.225
B com.	-0.022	-0.368	-5.079	.00***	1.452
A size.	0.004	0.054	0.637	.525	2.007
B age.	0.001	0.174	2.48	.014	1.357

$R^2 = .267$

$F(6,203) = 12.321***$

\* $p < .05$ , \*\* $p < .01$ , \*\*\* $p < .001$

The results of the standardized beta coefficients show the size of the impact of the two significant variables i.e., B div. and B com. on ROE. The magnitude of the impact of B com. is higher on the ROE compared to B div. in the Nepali commercial banks. Similarly, B size. and B ind. do not have a statistically significant role to play in increasing or decreasing the ROE. It is worth noting that, the beta coefficient of both B size. and B ind. are negative. Finally, the VIF values, less than five, of all the variables, especially predictors indicate no serious problem of multicollinearity in the regression model.

## DISCUSSION

The overall result regarding the impact of board characteristics on financial performance is consistent with the findings of Darmadi (2011); Al-Matari et al. (2012); Sobhan (2021); Nepal and Deb (2022). These scholarly works have reported the significant negative impact of board diversity and board-level committees on financial performance. They argued that the nominal representation of women in the boardroom and the lack of skills and professional experiences in the women involved have resulted in a negative impact on the accounting-based measures of financial performance. Further, the increased board committees have resulted in higher communication and management costs including the multi-task dilemma and decision-making bottlenecks, which have hindered the firm performance.

Similarly, the result of this study is in contrast to the findings of Carter et al. (2010); Acharya (2018). In their study, they reported the positive impact of board diversity and board committees on the ROA. Carter et al. (2010); Acharya (2018) have argued that board diversity and board committees enhance firm performance. Moreover, they stressed that such diversification and committee formation should not be solely driven by mandatory requirements of some Acts and the members should be selected based on their skills and professional expertise. Kanter (1987) states that when the number of minority members is low, they might be seen as representatives of the minority rather than valued for their unique skills and professional experiences, which could lead to role ambiguity and hinder their ability to enhance firm performance.

The findings of these scholarly works including the empirical analysis of this research help to establish the results reported in this study that the significant negative impact of board diversity and board-level committees on financial performance. Mainly is caused by the representation of members in the board and committees by tokenism or mandatory requirements of some Acts instead of skills and expertise in Nepali commercial banks.

## CONCLUSION

The current status of board characteristics and financial performance of commercial banks in Nepal showed that all commercial banks have strictly followed the mandatory provisions of Nepal Rastra Bank after BAFIA 2017 and have offered satisfactory average returns on assets and returns on equity in reference to the average returns of commercial banks reported by the Financial Stability Report (2022) published by NRB. It indicates that the current practices of board characteristics and returns offered to the assets and equity are satisfactory. The overall findings of the study indicated a statistically significant negative impact of board diversity and board committees along with the insignificant negative impact of board independence on the financial performance measured using ROA and ROE. The comprehensive outcome of this research points towards the presence of tokenism in the inclusion of women and independent directors in the boardroom of Nepali commercial banks. Furthermore, it highlights a tendency to prioritize compliance over performance, especially in regard to board committees. However, a focused study on these issues might be worthwhile.

The study on board characteristics and financial performance measured using ROA and ROE have policy implications for commercial banks and regulators. The study results revealed that the key concern of Nepali commercial banks towards compliance over performance especially in regard to board committees. There is no doubt that Nepali commercial banks need to strictly follow every regulatory provision made by Nepal Rastra Bank. However, banks should make a balance between adhering to regulatory requirements and prioritizing performance-related initiatives, for sustainable banking in Nepal.

The tokenism in the representation of women and independent directors is indicated by the study results. Thus, the regulator, however, is advised to review its policy relating to board diversity and board independence in a way that aligns the involvement of independent directors and women directors in the boardroom with the strategic direction and goals of the banks. There is a negative influence of board diversity and board committees on ROA and ROE. It implies that the banks need to address the

diversity issue not only in terms of numbers and proportion of gender representation but also in terms of qualification, experience, and skills so that firm performance increases. Further, in regard to board committees, banks are suggested to focus on the effectiveness of the committees formed rather than on the mandatory number of board committees. Thus, the banks as well as the regulator are advised to make policy reforms regarding the board committee composition and effectiveness.

In this study, financial performance was considered as the response variable and was proxied by ROA and ROE. These measures lack a comprehensive assessment of financial risk, market position, stability, and sustainability. The research scope for future studies can be the use of financial risk, financial stability, market-based measures, and sustainability as response variables that can add value for future research.

### **CONFLICT OF INTERESTS**

*The author has no conflicts of interest to disclose.*

### **ACKNOWLEDGEMENTS**

*This article draws upon the data from the Mini Research Grants-2023 (Award No.: MRN-04/CRI2023) funded by the Centre for Research and Innovation (CRI), Prithvi Narayan Campus, Pokhara. The author acknowledges the CRI for the research grant.*

### **REFERENCES**

- Abu, S. O., Okpeh, A. J., & Okpe, U. J. (2016). Board characteristics and financial performance of deposit money banks in Nigeria. *International Journal of Business and Social Science*, 7(9), 159-173.
- Acharya, S. (2018). *Improving corporate governance in Nepali financial institutions to promote growth and performance* [Unpublished doctoral dissertation]. The University of Waikato.
- Aguilera, R. V., Desender, K., Bednar, M. K., & Lee, J. H. (2015). Connecting the dots: Bringing external corporate governance into the corporate governance puzzle. *Academy of Management Annals*, 9(1), 483-573.
- Al-Matari, E. M., Al-Swidi, A. K., Fadzil, F. H., & Al-Matari, Y. A. (2012). The impact of board characteristics on firm performance: Evidence from nonfinancial listed companies in Kuwaiti Stock Exchange. *International Journal of Accounting and Financial Reporting*, 2(2), 310-332.
- Alodat, A. Y., Salleh, Z., Hashim, H. A., & Sulong, F. (2022). Corporate governance and firm performance: Empirical evidence from Jordan. *Journal of Financial Reporting and Accounting*, 20(5), 866-896.
- Arnwine, D. L. (2002, January). Effective governance: the roles and responsibilities of board members. *Baylor University Medical Center Proceedings*, 15(1), 19-22.
- Arora, A., & Sharma, C. (2016). Corporate governance and firm performance in developing countries: evidence from India. *Corporate Governance*, 2(1), 213-232.
- Arvanitis, S. E., Varouchas, E. G., & Agiomirgianakis, G. M. (2022). Does board gender diversity really improve firm performance? Evidence from Greek listed firms. *Journal of Risk and Financial Management*, 15(7), 306.

- Berle, A. A., & Means, G. C. (1932). *The modern corporation and private property*. Transaction Publishers.
- Brigham, E. F., & Ehrhardt, M. C. (2013). *Financial management: Theory & practice*. Cengage Learning.
- Brown L. & Caylor M. (2006). Corporate governance and firm valuation. *Journal of Accounting and Public Policy*, 25(4), 409-434.
- Carter, D. A., D'Souza, F., Simkins, B. J., & Simpson, W. G. (2010). The gender and ethnic diversity of US boards and board committees and firm financial performance. *Corporate Governance: An International Review*, 18(5), 396-414.
- Cheng, S. (2008). Board size and the variability of corporate performance. *Journal of Financial Economics*, 87(1), 157-176.
- Coles, J. L., Daniel, N. D., & Naveen, L. (2008). Boards: Does one size fit all? *Journal of Financial Economics*, 87(2), 329–356.
- Darmadi, S. (2011). Board diversity and firm performance: The Indonesian evidence. *Corporate Ownership and Control Journal*, 8(2) 234-251.
- Daily, C. M., Dalton, D. R., & Cannella Jr, A. A. (2003). Corporate governance: Decades of dialogue and data. *Academy of Management Review*, 28(3), 371-382.
- Economic Survey. (2022). *Economic survey 2021/22*. Ministry of Finance, Government of Nepal, 44-45.
- Eisenberg, T., Sundgren, S., & Wells, M. T. (1998). Larger board size and decreasing firm value in small firms. *Journal of Financial Economics*, 48(1), 35-54.
- Fama, E. F. (1980). Agency problems and the theory of the firm. *Journal of Political Economy*, 88(2), 288-307.
- Fama, E. F., & Jensen, M. C. (1983). Separation of ownership and control. *Journal of Law and Economics*, 26(2), 301-325.
- Freeman, R. E. (1984). *Strategic management: A stakeholder approach*. Pitman Publishing.
- Gafoor, C. A., Mariappan, V., & Thiyagarajan, S. (2018). Board characteristics and bank performance in India. *IIMB Management Review*, 30(2), 160-167.
- García-Ramos, R., & García-Olalla, M. (2011). Board characteristics and firm performance in public founder-and nonfounder-led family businesses. *Journal of Family Business Strategy*, 2(4), 220-231.
- Gadtaula, K. P., Gautam, H., & Agrawal, A. (2021). Impact of corporate governance on financial performance of commercial Banks in Nepal. *Manthan: Journal of Commerce and Management*, 8(2), 01-27.
- Green, S. B. (1991). How many subjects does it take to do a regression analysis. *Multivariate Behavioral Research*, 26(3), 499-510.
- GC, S. B. (2019). The effect of corporate governance and ownership structure on financial performance of listed companies in Nepal. *The Journal of Nepali Business Studies*, 12(1), 36-44.
- Habtoor, O. S. (2022). Board attributes and bank performance in light of Saudi corporate governance regulations. *Journal of Risk and Financial Management*, 15(3), 441-451.
- Haldar, A., Shah, R., Rao, S. N., Stokes, P., Demirbas, D., & Dardour, A. (2018). Corporate performance: does board independence matter? Indian evidence. *International Journal of Organizational Analysis*, 13(2)67- 83.

- Hamid, N., & Purbawangsa, I. B. A. (2022). Impact of the board of directors on financial performance and company capital: Risk management as an intervening variable. *Journal of Co-Operative Organization and Management*, 10(2), 150-164.
- Hillman, A. J., & Dalziel, T. (2003). Boards of directors and firm performance: Integrating agency and resource dependence perspectives. *Academy of Management Review*, 28(3), 383-396.
- Jackling, B., & Johl, S. (2009). Board structure and firm performance: Evidence from India's top companies. *Corporate Governance: An International Review*, 17(4), 492-509.
- Jan, S., & Sangmi, M. (2016). The role of board of directors in corporate governance. *Imperial Journal of Interdisciplinary Research*, 2(5), 707-715.
- Jensen, M. C., & Murphy, K. J. (1990). Performance pay and top-management incentives. *Journal of Political Economy*, 98(2), 225-264.
- Kanter, R. M. (1987). Men and women of the corporation revisited. *Management Review*, 76(3), 14-32.
- Kathuria, P., & Dash, G. (2016). Board size and corporate financial performance: an investigation. *Vikalpa*, 24(3), 11-17.
- Khatab, H., Masood, M., Zaman, K., Saleem, S., & Saeed, B. (2011). Corporate governance and firm performance: A case study of Karachi stock market. *International Journal of Trade, Economics and Finance*, 2(1), 39-52.
- Kirchmaier, T., & Gerner-Beuerle, C. (2021). *Corporate Governance in South Asia: Trends and Challenges*. Asian Development Bank.
- Lipton, M., & Lorsch, J. W. (1992). A modest proposal for improved corporate governance. *The Business Lawyer*, 59-77.
- Mishra, R. K., & Kapil, S. (2018). Effect of board characteristics on firm value: evidence from India. *South Asian Journal of Business Studies*, 7(1), 41-72.
- Nepal, M., & Deb, R. (2022). Board characteristics and firm performance: Indian textiles sector panorama. *Management and Labour Studies*, 47(1), 74-96.
- Orozco, L. A., Vargas, J., & Galindo-Dorado, R. (2018). Trends on the relationship between board size and financial and reputational corporate performance: The Colombian case. *European Journal of Management and Business Economics*, 13(2), 56-69.
- Pfeffer, J., & Salancik, G. (1978). *The External Control of Organisations, A Resource Dependence Perspective*. Harper and Row.
- Pucheta-Martínez, M. C., & Gallego-Álvarez, I. (2020). Do board characteristics drive firm performance? An international perspective. *Review of Managerial Science*, 14(6), 1251-1297.
- Rashid, A., De Zoysa, A., Lodh, S., & Rudkin, K. (2010). Board composition and firm performance: Evidence from Bangladesh. *Australasian Accounting Business and Finance Journal*, 4(1), 76-95.
- Ross, S. A., Westerfield, R., & Jordan, B. D. (2008). *Fundamentals of corporate finance*. Tata McGraw-Hill Education.
- Sobhan, R. (2021). Board characteristics and firm performance: Evidence from the listed non-banking financial institutions of Bangladesh. *International Journal of Management, Accounting & Economics*, 8(1), 25-41.



- Subramanian, S. (2015). Corporate governance, institutional ownership and firm performance in Indian state-owned enterprises. *Asia-Pacific Journal of Management Research and Innovation*, 11(2), 117-127.
- Terjesen, S., Aguilera, R. V., & Lorenz, R. (2015). Legislating a woman's seat on the board: Institutional factors driving gender quotas for boards of directors. *Journal of Business Ethics*, 128(2), 233-251.
- Trochim, W. M. (2005). *Research methods: The concise knowledge base*. Atomic Dog Publishing.
- Yermack, D. (1996). Higher market valuation of companies with a small board of directors. *Journal of Financial Economics*, 40(2), 185-211.