CORPORATE GOVERNANCE AND FIRM PERFORMANCE IN SAUDI ARABIA

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A Thesis Submitted in Fulfilment of the Requirements for the Degree of Doctor of Philosophy

Faculty of Business and Law
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Statement of Originality

The thesis contains no material which has been accepted for the award of any other degree or diploma in any university or other tertiary institution and, to the best of my knowledge and belief, contains no material previously published or written by another person, except where due reference has been made in the text. I give consent to the final version of my thesis being made available worldwide when deposited in the University’s Digital Repository**, subject to the provisions of the Copyright Act 1968.

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Ashraf M. Alsahafi
16-01-2017
Dedication

I dedicate this thesis to the memory of my father who sadly passed away during my study.
Acknowledgment

All the praises and thanks be to Allah, the Almighty, who has given me the strength, patience and knowledge to complete this thesis.

I would like to take this opportunity to extend my thanks and appreciation to every individual who lent me a helping hand and gave me support during my study. I would like particularly to express my special thanks to my supervisors Prof. Jim Psaros and Dr. Paul Docherty for their valuable guidance, encouragement and support throughout my research. Their valuable time spent on reading with prompt feedback, insightful comments and generous response to every request for guidance during my study have been much appreciated. I am very grateful for the opportunity to work with them as I have learned a great deal from their knowledge and experience. Without their contributions, I would not have been able to accomplish this thesis.

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I would like to express my heartfelt feelings to my mother for her love, prayers and wishes for Godspeed and success. My very special thanks go to my beloved family, my wife, Nisreen, who always supported and motivated me at every stage of this study, and my children, Ziyad and Rola, for their unending patience and tolerance over the period of the study. Without their love and support, this thesis would never have reached a conclusion.
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<tr>
<td>AGE</td>
<td>Firm Age</td>
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<tr>
<td>BIND</td>
<td>Board Independence</td>
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<td>BSZ</td>
<td>Board Size</td>
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<td>CAPEX</td>
<td>Capital Expenditure</td>
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<td>CEO</td>
<td>Chief Executive Director</td>
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<td>CEO Duality</td>
<td>CEO Duality</td>
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<td>CEOT</td>
<td>CEO Tenure</td>
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<td>CG</td>
<td>Corporate Governance</td>
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<td>CGRs</td>
<td>Corporate Governance Regulations in Saudi Arabia</td>
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<td>CMA</td>
<td>Capital Market Authority in Saudi Arabia</td>
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<tr>
<td>DV</td>
<td>Dependent Variable</td>
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<tr>
<td>DY</td>
<td>Dividend Yield Ratio</td>
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<tr>
<td>DZIT</td>
<td>Department of Zakat and Income Tax</td>
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<tr>
<td>EBIT</td>
<td>Earnings Before Interest and Tax</td>
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<tr>
<td>EPS</td>
<td>Earnings per Share</td>
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<td>EVA</td>
<td>Economic Value Added</td>
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<td>FAM</td>
<td>Family Ownership</td>
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<td>FCEO</td>
<td>Family CEO</td>
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<td>FE</td>
<td>Fixed Effects Regression</td>
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<td>FG</td>
<td>Firm Growth</td>
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<td>G20</td>
<td>The Group of Twenty</td>
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<td>GCC</td>
<td>Gulf Cooperation Council</td>
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<td>GDP</td>
<td>Gross Domestic Product</td>
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<td>Government Ownership</td>
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<td>Industry</td>
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<td>Islamic Financing</td>
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<td>IV</td>
<td>Independent Variable</td>
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<td>LD</td>
<td>Long-term Debt Ratio</td>
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<td>LEV</td>
<td>Leverage Ratio</td>
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<td>LM</td>
<td>Breusch-Pagan Lagrange Multiplier</td>
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<td>MAN</td>
<td>Managerial Ownership</td>
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<tr>
<td>MCI</td>
<td>The Ministry of Commerce and Industry</td>
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<td>MTB</td>
<td>Market to Book Ratio</td>
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<tr>
<td>NPM</td>
<td>Net Profit Margin</td>
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<tr>
<td>OECD</td>
<td>Organization of Economic Co-operation and Development</td>
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<td>OLS</td>
<td>Ordinary Least Square</td>
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<tr>
<td>OPEC</td>
<td>Organization of the Petroleum Exporting Countries</td>
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<tr>
<td>Abbreviation</td>
<td>Full Form</td>
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<tr>
<td>OROA</td>
<td>Operating Return on Assets</td>
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<td>OWN</td>
<td>Ownership Concentration</td>
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<td>PE</td>
<td>Price to Earnings</td>
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<td>Q</td>
<td>Tobin's Q</td>
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<tr>
<td>ROA</td>
<td>Return on Assets</td>
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<td>ROE</td>
<td>Return on Equity</td>
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<tr>
<td>ROIC</td>
<td>Return on Invested Capital</td>
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<tr>
<td>ROS</td>
<td>Return on Sales</td>
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<td>SABIC</td>
<td>Saudi Basic Industries Corporation</td>
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<tr>
<td>SD</td>
<td>Short-term Debt Ratio</td>
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<tr>
<td>SOCPA</td>
<td>The Saudi Organization for Certified Public Accountants</td>
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<tr>
<td>STC</td>
<td>Saudi Telecom Company</td>
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<tr>
<td>STD</td>
<td>Standard Deviation</td>
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<td>TD</td>
<td>Total Debt Ratio</td>
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<tr>
<td>UAE</td>
<td>The United Arab Emirates</td>
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<tr>
<td>VIF</td>
<td>Variance Inflation Factor</td>
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<td>The World Trade Organization</td>
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Abstract

Corporate governance in a specific country relates systematically to its social, economic and legal structures. From this standpoint, and since Saudi Arabia has unique cultural, economic and political features, this study aims to explore corporate governance practices in Saudi Arabia. A close look at the influence of these features on the Saudi business environment reveals that agency theory is not the appropriate theory that can be applied in the Saudi context, despite its widespread adoption in the extant studies of corporate governance. Alternatively, stewardship theory seems to be the most relevant theory to the Saudi business environment. Therefore, stewardship theory is adopted as the main theoretical framework for this study, augmented with other theories including stakeholder, resource dependency and institutional theories.

Taking these multiple theoretical frameworks as a key point of departure from previous studies, this thesis seeks to examine the relationship between corporate governance and firm performance, focusing on three main areas: board of director characteristics, ownership structure and capital structure. The study uses secondary data obtained from annual reports of all non-financial listed firms in Saudi Arabia over a six-year period from 2009 to 2014. Multiple performance measures including both accounting-based and market-based measures are adopted. A number of firm characteristics including firm size, age, growth, capital expenditure, leverage and industry are employed as control variables. The study utilises quantitative analysis techniques including both descriptive and inferential statistics such as ANOVA, t-tests and regression analysis. A lagged structure method is also employed to address endogeneity problems.

The findings of this study, in terms of accounting-based measures of performance, indicate the existence of a relationship between firm performance and the three areas of focus in the directions that would be expected when examining the impact of corporate governance through the lenses of stewardship theory and resource dependency theory. The results related to the board of director characteristics indicate that while there is a negative relationship between board independence and firm performance, other board characteristics, namely board size, CEO duality, CEO tenure and family CEO, are positively associated with firm performance. Regarding ownership structure, the results reveal a positive relationship between ownership concentration and firm performance. Among the types of ownership, only family and managerial ownership have a positive impact on firm performance. Interestingly, family ownership is found to have a positive impact on firm performance only when family owners are on the board of directors. With respect to capital structure, the findings indicate a negative relationship between capital structure and firm performance. In addition, the study reveals a positive impact of Islamic debt on firm performance. On the other hand, the results based on market-based measures of performance show no significant impact of the board of director characteristics, ownership structure and capital structure on firm value.

In light of the recent adoption of the OECD principles of corporate governance across a range of emerging markets, a key implication of this thesis is that such regulations may need to be refined to better reflect the specific context of the countries within which they operate. The findings of this study provide valuable implications for policymakers, regulators, firms, shareholders and investors in Saudi Arabia.