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Board Characteristics and Financial Performance of Selected Listed Non-Financial Firms in Nigeria

Racheal, E. ABUSOMWAN (Ph.D) *; Nse, UMOH-DANIEL [1]; Onyinyechi Emmanuella, ANI-EJIOFOR [2]

Department of Accounting,
Benson Idahosa University, Benin City, Nigeria.

* rabusomwan@biu.edu.ng; [1] ndaniel@biu.edu.ng; [2] aniejioforonyinyechi@gmail.com

* Correspondence Author

Abstract

Research Objective: The study aimed to evaluate the effect of board characteristics on the financial performance of selected listed non-financial firms in Nigeria.

Methodology: The research analysed data from thirty (30) listed non-financial firms over a ten-year period (2013-2022) using a panel data regression model with a random effect approach.

Findings: Results revealed that board size is insignificantly and negatively related to financial performance, board independence shows an insignificant positive relationship, and board gender diversity has a significant negative effect on financial performance.

Conclusion: The study concludes that the impact of board characteristics on financial performance varies across different variables, potentially due to industry-specific factors.

Recommendations: Further investigation into board characteristics is recommended to better understand their influence on firm performance.

Key words: *Board characteristics, board independence, board gender diversity, financial performance, non-financial firms.*

1.0 Introduction

Boards in any establishment whether public or private, quoted or unquoted, profit oriented or not, is the apex decision making organ of the establishment (Datta, 2018). In the corporate world, the Board of Directors of a company is the representative of shareholders and as such has a responsibility to ensure the efficient management of the entire organisation (Arumona, 2017). According to Arumona (2017) financial performance is the yield or the results of activities carried out in relation to the purposes being pursued.

For firms to enjoy high performance, the independence of the board of directors in any organisation cannot be overemphasized. The board should be structured and composed in

such a way that it will act to monitor its own activities. However, countries like the United Kingdom and Nigeria have the positions of the corporate chairman and that of the chief executive officer (CEO) separated in most cases (Kabiru, 2022). This separation enables a check and balance system (Alhassan & Boakye, 2020).

Board size also aids effectiveness and improves firm performance (Onuorah & Imene, 2016). According to Mohammed and Buhari (2019) board size affects the quality of contemplation among members and ability of the board to agree at optimal corporate decisions. Therefore identifying the appropriate board size is essential because size can be inimical to corporate governance effectiveness beyond optimal level. However, determining an appropriate size of the board has been an issue of debate in corporate governance literature.

Another vital component of board characteristics is board gender diversity. It became an important issue for almost all of the organisations due to the increase in the percentage of female employees. In addition, broad gender diversity adds to the range of perspectives in decision making processes, also a larger representation of women can introduce new approaches, views and beliefs (Rao & Tilt, 2016). Premised on the foregoing, the major aim of this study was to establish the effect of board characteristics on financial performance of non-financial listed firms in Nigeria.

Conceptual Review

Financial Performance

A wide variety of corporate performance definitions have been introduced in the literature. Financial performance is the firms' ability to generate resources sufficient for its day-to-day operations over a given period (Yu & Ashton, 2015). It examines the overall financial health of a business over a given period of time and can be used to contrast the performance of identical firms in similar industries or between industries in general (Atrill, 2005).

Return on Assets

ROA is one of the profitability ratios used to measure the effectiveness of the company in generating profits by utilising the total assets it has. As one of the most important profitability ratios and indicators of financial performance regarding a firm's resources and assets, it is useful for comparing rival companies in the same industry (Saeid & Soleimani 2012). It is calculated by dividing net profit by total assets. Calculating accounting profit considering the price volatility may make difficult decision making for the firm`s performance evaluation (Saeid & Soleimani 2012).

However, in recent year’s economic situation has changed financial performance measurement evaluation. One of financial performance measurement evaluation is ROA. ROA evaluates a firm's ability in profit making according to total investments in assets. Return on Assets (ROA) is a ratio that shows the results of the total assets used in the company (Kasmir, 2014). The greater the ROA, the higher the company's ability to provide

profits through assets owned by the company and vice versa, low ROA can be caused by the number of idle company assets, too much investment in inventory, excess paper money, fixed assets operating below normal and others. Syardian, (2015) states that ROA is a ratio that shows the company's ability to generate net income by using total assets. The greater the ROA results, the better the company's performance.

Board Characteristics

Board Size

Board size plays an important role in the Directors capacity to monitor and control managers (Lipton, 2013). Complications may arise in organising and coordinating large groups of directors due to the board size which is completely related to the board's ability to advise and engage in long- term strategic planning. This is based on the belief that larger boards are better for business performance because they have a wider range of experience to assist make better decisions and are more difficult to control by a dominant chief executive officer (CEO) (Angahar & Mejabi, 2014). A study by (Dogan & Yildiz, 2013) shows that a larger board size led to better decision making, effectiveness in monitoring financial performance, managing risk and providing diversity that could assist companies in securing resources and reduction of environmental uncertainties.

H_{O1}: Board size does not have significant effect on the financial performance of selected non-financial firms

Board Independence

A board of directors is considered desirable and can be defined as "independent" just when it's made up of at least 50% independent directors (Klein, 2002. Although board independence may have a positive effect on a company's profitability. In some cases, these advantages are found only among large companies, whose financial resources make it easier to recruit expert independent directors compared to smaller companies (Miletkov, 2015).

H_{O2}: Board independence does not have significant effect on the financial performance of selected non-financial firms

Board Gender Diversity

Board diversity entails ethnicity, age, location, education, gender, independence, skills, knowledge, and experience of the members (Fraga & Silva, 2012). Extant studies in favour of diversity highlight the benefits both in terms of efficiency and better monitoring. Diversity (of gender, nationality, age, professional background) is deemed to widen the debate within the boards and help to avoid the possibility of group thinking; increase creativity and innovation; improve problem solving; promote the exchange of ideas, providing new insights and perspectives to the board, Schippers (2019).

H_{O3}: Board gender diversity does not have significant effect on the financial performance of selected non-financial firms

2.0 Empirical Review

Board Size and Financial Performance

Board size affects the quality of deliberation among members and ability of board to arrive at optimal corporate decisions. However, determining an ideal size of the board has been an ongoing and controversial debate in corporate governance literature. Several arguments arise in the literature on whether the size of corporate boards determines corporate performance. Chang et al. (2012), Esa and Mohd-Ghazali (2012) provide evidence of a positive relationship between board size and corporate performance. Based on the positive findings, Esa and Mohd-Ghazali (2012) argued that larger boards offer more knowledge and experience and also put forward different ideas in board deliberations. Similarly, Haji and Mohd-Ghazali (2013) concluded that large board size is connected with increased monitoring capacity which could lead to sharing of a variety of experiences in boardrooms. Besides, a corporate governance-sustainability disclosure study conducted on a sample of 50 Pakistan companies by Lone, Ali, and Khan (2016) established that a large number of directors on corporate boards bring the experiences of diverse backgrounds which affect the level of corporate performance. More recently, Sadou, (2017) highlighted that larger boards are more effective and have greater influence over companies' performances. On the other side, some literature provided evidence of a negative association between board size and sustainability disclosure. In Nigeria, the rule guiding the size of a corporate board is spelled out in the country's corporate governance code. Specifically, the revised code of corporate governance 2018 stipulates that corporate board size should be relative to the complexity and scale of companies' operations. The code further specifies that the number of directors in a company's board should not fall below five (5). However, the governance code did not specify the maximum number of directors a company should appoint for any specified period. Therefore, considering the provision in Nigeria's revised corporate governance code, this study expects board size to have a positive effect on corporate performance.

Board Independence and Financial Performance

The presence of independent directors on a board can help to segregate the management and control tasks of a company and this is expected to offset inside members' opportunistic behaviours (Jensen and Meckling, 1976 cited in Hussain et al., 2016). In addition, independent directors generally have stronger and extended engagement with wider groups of stakeholders (Wang and Dewhirst, 1992), and they tend to have a broader perspective that is likely to result in a greater exposure to performance requirements Rupley, (2012). However, despite several support for independent directors on corporate boards, debates were still ongoing whether independent directors are a mechanism for aligning managerial interests with those of shareholders and also their value creation merits for corporate performance.

Huang (2010) concluded that independent directors act as a monitoring mechanism that ensures companies are properly managed by corporate management and also work towards enhancing corporate image and performance. A study conducted on sampled US firms by Zhang, Zhu, and Ding (2013) claims that independent directors have more diverse backgrounds and represent external stakeholders of companies. As such, they have a stronger orientation towards better operation strategies than their counterparts in the boardroom. Studies Sharif and Rashid (2014), Kaur, (2016) indicated a positive link between board independence and improved corporate performance. Michelon and Parbonetti (2012), Janggu et al. (2014) provided evidence of an insignificant relationship between independent directors and improved corporate performance. This suggests that board independence does not seem to play a vital role in improving or determining a firm's extent of performance. Based on the insignificant result observed, managers are perceived as moral agents other than opportunistic individuals. As such, their role is to achieve a balance between the interests of diverse stakeholders Bello and Kamarul, (2017). Therefore, it is presumed that a corporate board with a higher proportion of independent directors will ensure improved board monitoring quality and also work toward satisfying the needs of all stakeholders. Therefore, based on the positive result observed in the extant literature, this study anticipates a significant positive relationship between board independence and financial performance. This implies that with a higher proportion of independent directors on a corporate board, a company will exhibit more concern and give more attention to corporate performance

Board Gender Diversity and Financial Performance

The number of studies on board gender diversity and firm performance from different countries has increased in recent years because of the unique knowledge, information and variety of experiences, skills and networks of gender-diverse boards (Hillman, 2007; Miller & Triana, 2009). A board with female members is more able to integrate the interest of multiple stakeholders, including employees, customers, suppliers and the communities with the performance-based interests of shareholders (Harrison and Coombs, 2012). This argument is supported by Smith et al. (2006) cited in Vo and Phan, (2013), who considered three different reasons to recognize the importance of females on a board. First, female board members usually have a better understanding of a market in comparison with male members. As such, this understanding will enhance the decisions made by the board. Second, female board members will bring better images in the perception of the community for a firm and this will contribute positively to the firm's performance. Third, other board members will have enhanced understanding of the business environment when female board members are appointed. Hence, as a result of women on board, a firm’s performance is improved directly and indirectly. Low, Roberts and Whiting (2015) investigated Asian firms in Hong Kong, South Korea, Malaysia and Singapore and found that the appointment of female directors can positively affect the firm’s performance. Rao and Tilt (2016) conducted a comprehensive review of prior board diversity and overall corporate performance.

In the context of Nigeria, culture plays a pivotal role in restricting women's participation in corporate boards. However, this perception is gradually fading out. As such the significance of gender diversity is nowadays becoming obvious and visible (Şener and Karaye, 2014). An example is the recent measure put in place by the Central Bank of Nigeria (CBN) to boost female representation in board formation in the country. The CBN through its banker's committee imposes a mandatory quota target on deposit money banks. The aim is to increase women's representation on companies' boards to 30 percent (Şener and Karaye, 2014). Therefore, considering the recent changes in Nigerian gender diversity policies and also the view of stakeholder theory which supports a positive association between board diversity and firm performance, this study expects women on board to have a positive and significant effect on firm performance.

Theoretical Review

Agency Theory

This study uses the agency theory as a theoretical background to form an empirical framework for assessing board characteristics and firm performance of non-financial listed companies in Nigeria. In examining the effect of board characteristics on firms in Nigeria, the agency theory is relevant because an agency relationship exists between the board who act on behalf of the firm and its shareholders. Framework for assessing board composition and firm performance of selected listed companies in Nigeria. Agency theory was developed by Jensen and Meckling (1976). They suggested a theory of how the governance of a company is based on the conflicts of interest between the company's owners (shareholders), and its managers. Each of these groups has different interests and objectives. Agency theory can be defined as the relationship between the shareholders and the company executives or managers. This theory assumes that managers are self-interested and risk averse. Agency theory has dominated the corporate governance research and provides the system on how a board monitors management on behalf of the shareholders. The separation of control and ownership leads to misalignment of manager's interest to shareholders interest. Agency theory states that one of the major functions of the manager is to align the companies' interest with shareholders interest and identifies the agency relationship with one party, the principle who delegates work to another party, the agent.

In respect to board size, agency theory states that larger board size equates to more effective monitoring of management by reducing the domination of the CEO on board and therefore leads to greater firm's performance. According to agency theory, the board of directors monitors management to prevent them from engaging in actions that are likely to benefit them and not the shareholders. Larger boards can be more effective as the workload of monitoring managers can be divided over a greater number of individuals. On the other hand, agency problems can become more severe with a larger board, and hence, it becomes easier for the managers to influence and control the board. This theory suggests that a larger board can

cause coordination and communication issues, thus allowing short-term profit-oriented managers to take control.

Also as regards to board independence, agency theory advocates the usage of independent directors because of their ability to monitor management. The agency theory suggests that the presence of non- executive directors on the board is a crucial element in ensuring the managers will act in the best interest of shareholders.

With regard to board gender diversity, agency theory is mainly concerned about monitoring the role of directors. Representation from different groups will provide a balanced board so that no individual or group of individuals can dominate the decision making of the board. Gender diversity is connected with effectiveness in the oversight function of the board of directors. The oversight function may be more effective if there is gender diversity on board which allows for a broader range of opinions to be considered.

3.0 Methodology

The research design adopted in this study is ex-post facto. In line with Okoro and Ihenyen, (2020) this design is less time consuming and affordable as it utilises data that already exist and it does not involve the researcher's direct control. Secondary data was used for this study. The data was obtained from corporate annual reports of the sampled non-financial firms listed on the Nigerian exchange group from 2013-2022 financial years.

Model Specification

The regression model to test the relationship between board characteristics and financial performance is as follows:

$ROA = \beta_0 + \beta_1(BS_1) + \beta_2(BI_2) + \beta_3(BG_3) + \varepsilon_{it}$

Where:

ROA = Return on Assets, the dependent variable

β_0 = intercept

BS = Board Size

BI = Board independence

BG = Board gender

$\beta_{1....}B_3$ = coefficients

ε= Error term, i = cross sectional of the vector of the variables, t = time series

Table 1. Operationalization of variables

The variables were measured as follows:

S/N	VARIABLES	TYPES OF VARIABLES	MEASUREMENT	SOURCE	APRIOR SIGN

1.	Financial performance proxied by: Return on assets. (ROA)	Dependent	This is measured as profit before tax divided by total assets. = profit before tax (PBT)/ Total assets	Godwin, (2019), Abiodun and Dorothy, (2020)	
2.	Board characteristics proxied by: Board size (BD)	Independent	Total number of members sitting on the board.	Abayomi, (2020) Halima, (2022)	-
3.	Board independence (BI)	Independent	Ratio of non- executive directors to the total number of directors.	Abayomi, (2020) Halima, (2022)	+
4.	Board gender diversity	independent	Ratio of female directors to total number of directors	Godwin, (2019) Haruna, (2021)	+

Presentation and Analysis of Results

Table 1 Descriptive Statistics

	ROA	BS	BI	BGD
Mean	1.958041	13.43212	3.142621	3.082327
Median	2.002784	13.49943	3.100993	2.995732
Maximum	6.686122	20.40718	4.438052	5.298317
Minimum	-4.55305	8.317766	1.965713	2.039921
Std. Dev.	1.202247	1.703199	0.529657	0.570575
Skewness	-0.54736	0.110342	0.211869	0.563079

Kurtosis	6.393393	4.214766	2.716885	3.878521
Jarque-Bera	158.9188	19.05449	3.246359	22.10033
Probability	0.000000	0.000073	0.19727	0.000016
Sum	587.4124	4029.636	942.7862	801.405
Sum Sq. Dev.	432.1737	867.3648	83.88049	84.31899
Observations	300	300	300	260

Source: Author's Compilation Using EViews 10

Descriptive statistics of the variables are reported in Table 1. The ROA is used to measure the financial performance with a mean of 1.958041 this means that the companies have an average of 1.958041 return on asset and a minimum of -4.55305 while the maximum is 6.686122 also the Jarque Bera stood at 158.9188. The probability stood at 0.000000. The board size is measured based on the number of members sitting on the board. The board size averages 13.43212 this indicates that on the average the size of the board of the sampled Commercial bank firms is 13.43212. The minimum is 8.317766 while the maximum is 20.40718. A standard deviation of 1.703199 confirms variability in the size of the board and The Jarque Bera stood at 19.05449 while probability stood at 0.000073. Board independent averages 3.142621 with a median of 3.100993 it also shows that a minimum of 1.965713 and a maximum of 4.438052 board members are independent and The Jarque Bera stood at 3.246359. The probability stood at 0.19727. Board gender revealed a mean of 3.082327 as well as a minimum 2.039921 this means that some firms have at least 2 female members on the board it also shows a maximum of 5.298317 and The Jarque Bera stood at 22.10033. The probability stood at 0.000016. This study uses the analysis of skewness for normality tests. ROA, BS, BI, BGD have a skewness of -0.54736, 0.110342, 0.211869, 0.563079. This means that the variables follow a normal distribution.

Table 2: Correlation Matrix and Covariance Analysis

	ROA	BS	BI	BGD

ROA	1			
BS	-0.048000	1		
BI	0.166467	0.201571	1	
BGD	0.141715	-0.30135	0.078583	1

Source: *Author's Compilation Using EViews 10*

The significance level of this result is indicated in table 2. The coefficient of correlations between ROA and BS is -0.048000. This implies that board size is statistically negatively significant to financial performance. In addition, the result also shows that BI is 0.166467 correlated with ROA. This implies that a positive but statistically insignificant relationship exists between board independence and financial performance of the sampled companies. The coefficient value for BGD stands at 0.141715, this indicates that there is a positive but statistically insignificant correlation between board gender and financial performance of the sampled companies. The finding shows that there is a correlation between all variables.

Table 3 Variance Inflation Factor Test

Variable	Coefficient Variance	Uncentered VIF	Centred VIF
C	1.090036	333.9178	NA
BS	0.004159	232.7243	1.034491
BI	0.030657	94.86522	1.124522
BGD	0.029642	87.37047	1.099188

Source: *Author's Compilation Using EViews 10*

The variance inflation factor revealed that there is no problem of multicollinearity as the centred VIF is 1.034491, 1.124522, and 1.099188. There will be no problem of multicollinearity if the centred VIF is 1 to 10.0

Table 4 Heteroskedasticity Test

Heteroskedasticity Test: Breusch-Pagan-Godfrey

F-statistic	5.711136	Prob. F(3,256)	0.0008
Obs*R-squared	16.30956	Prob. Chi-Square(3)	0.0010
Scaled explained SS	44.37140	Prob. Chi-Square(3)	0.0000

Source: *Author's Compilation Using EViews 10*

The Heteroskedasticity Breush-Pagan test measures how errors increase board size, board independence, board gender diversity. The test assumes the error variances are due to a linear function of independent variables in the model. The test will assume that the error of no heteroskedasticity exists if the F-Statistic value is above 0.05 and assume that heteroskedasticity error exists if the p value (Prob. F) is below 0.05. In this case, the p. value revealed 5.711136 > 0.05, R-square value at 16.30956. Therefore, no heteroskedasticity exists in the data.

Table 5 Hausman Test

Correlated Random Effects - Hausman Test

Equation: Untitled

Test cross-section random effects

Test Summary	Chi-Sq. Statistic	Chi-Sq. d.f.	Prob.
Cross-section random	9.910949	3	0.0193

Source: *Author's Compilation Using EViews 10*

The Hausman test is used as a test to determine the right model between the fixed and random effects model. Random effects model is appropriate if the Probability value is greater than 5% while fixed effects model is appropriate if the probability value is less than 5%. The

probability value here is 0.0193 which is less than 5% thereby we do not accept the null hypothesis and conclude that the fixed effects model is appropriate.

Table 6 Regression Results

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	3.169364	1.044048	3.035650	0.0027
BS	-0.020874	0.064492	-0.323664	0.7465
BI	0.040374	0.175090	0.230591	0.8178
BGD	-0.351220	0.172169	-2.039973	0.0425
	Effects Specification			
Cross-section fixed (dummy variables)				
R-squared	0.503822	Mean dependent var	1.932865	
Adjusted R-squared	0.436359	S.D. dependent var	1.227117	
S.E. of regression	0.921271	Akaike info criterion	2.788692	
Sum squared resid	193.5127	Schwarz criterion	3.226930	
Log likelihood	-330.5300	Hannan-Quinn criter.	2.964870	
F-statistic	7.468135	Durbin-Watson stat	1.578560	
Prob(F-statistic)	0.000000			

Source: *Author's Compilation Using EViews 9.0*

The hypothesis for this study was tested at the 5% significance level. The decision rule was to accept the null hypothesis if the p-value is greater than 0.05, otherwise, the alternative hypothesis was accepted and vice versa. The hypotheses were as follows:

$H0_1$: Board size does not have a significant effect on the financial performance of listed non-financial firms in Nigeria.

Board size which was measured based on the number of members on the board was found to be negative and non-significant at a 5% significant level therefore we reject the null hypotheses.

$H0_2$: Board independence does not have a significant effect on the financial performance of listed non-financial firms in Nigeria.

The study observed that board independence has no significant effect on financial performance therefore we accept the null hypotheses.

$H0_3$: Board gender diversity does not have a significant effect on the financial performance of listed non-financial firms in Nigeria.

The study observed that gender diversity which was measured based on the ratio of female to male members of the board has a negative but significant effect on financial performance therefore we do not accept the null hypothesis.

Discussion of Findings

Specifically, the study found out that board size has a negative but non-significant effect on financial performance in Nigeria. This is inconsistent with the works of Yermack, (1996) who found a significant relationship as well as Fama and Jensen (1983). A negative relationship implies that as the size of the board increases, financial performance reduces. On the contrary, the findings in this study are consistent with the findings in Odudu, and Okpe (2016) who concluded that board size has no significant effect on financial performance of listed non-financial companies.

The study also found out that board independence has a positive and non-significant effect on financial performance in Nigeria. A positive relationship means that the independence of the board improves financial performance. This is inconsistent with the findings of (Knyazeva, & Masulis, 2013; Wei, & Yang, 2015) who documented a negative association between board independence financial performance in Nigeria. But, the work of Sharif and Rashid (2014) and Kaur et al., (2016) indicated a positive link between board independence and improved corporate performance.

Finally this study found board gender diversity has a negative but significant effect on financial performance in Nigeria. This is inconsistent with the works of Wang and Clift (2009) where there is no strong relationship between gender diversity on the board and financial performance. Roberts and Whiting (2015) investigated Asian firms in Hong Kong,

South Korea, Malaysia and Singapore and found that the appointment of female directors can positively affect the firm's performance. Conversely, Adams and Ferreira (2009) and Pletzer, Nikolova, Kedzior, and Voelpel (2015) highlighted a negative relationship between female directors and firm performance due to these directors' lack of skills and experiences in monitoring the performance of their firms. Strydom, Au Yong, and Rankin (2016) found that board gender diversity may not affect firm performance in terms of earnings quality.

4.0 Conclusion

The study aimed at detecting the effect of board Characteristics on financial performance of listed non-financial firms in Nigeria. The study focused on examining the independent variables such as board size, board independence, and board gender diversity. The panel data regression model was used to analyse the data for the study and the study adopted the use of random effects. An understanding of the factors that could significantly affect financial performance, and strict adherence to the rules governing those factors, would inadvertently increase the possibility of improved financial performance. This would in turn boost the confidence of investors, while at the same time enhancing the discovery and reporting of the board. This leads to an improved role of the directors, and their possible impact to the business environment is enhanced.

Based on the findings derived, the study concludes that there are several characteristics that affect financial performance. However, the impact tends to vary among the different variables investigated. This can be as a result of the variance among firms and the particular industries used for the study.

Recommendation

Based on the findings made in the study, the following recommendations were made:

Firstly, there is a need for smaller board sizes accompanied by skill, experience and expedience of the board which will help to boost financial performance. Secondly, board independence and board diversity as a board attribute are key factors to be considered by the shareholders in order to improve the performance of such a firm because these two variables both have positive and statistically significant effects on firm performance. Thirdly, organisations are encouraged to have more female members on the board in order to enhance board gender diversity needed to improve customer satisfaction. Therefore, an inclusion of females in the board membership should be encouraged.

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