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The Role of Corporate Governance on the Market Value of the Firms: A Case Study of Industrial and Investment Companies Listed in the Palestine Exchange

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M A K A L E B İ L G İ S İ

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ÖZ

Bu makalenin amacı, Filistin borsasında işlem gören hem sanayi hem de yatırım sektörlerindeki şirketlerin kurumsal yönetim ile piyasa değeri arasındaki neden-sonuç ilişkisini incelemektir. Veriler 2013 – 2019 dönemine ait yıllık finansal raporlardan ve şirketlerin web sitelerinden toplanmıştır. Kurumsal yönetimin şirket performansı üzerindeki neden ve etki ilişkisini araştırmak için içerik analizi ve panel veri analizi kullanılmıştır. Sonuçlar, Filistin borsasında işlem gören sanayi şirketlerinin piyasa değeri üzerinde cinsiyet çeşitliliği için olumlu bir neden-sonuç ilişkisi olduğunu göstermiştir. Bu arada, kurumsal yönetim boyutunun tamamı Filistin borsasında işlem gören yatırım şirketlerinin piyasa değeri için önemsizdi. Dolayısıyla kurumsal yönetimin yatırım şirketlerinin piyasa değeri üzerinde hiçbir etkisi yoktur.

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A B S T R A C T

The purpose of this paper is to examine the cause-and-effect relationship between corporate governance and the market value of companies in both the industrial and the investment sectors listed in the Palestinian stock exchange market. The data was collected from the annual financial reports and the websites of the companies for the period from 2013 – 2019. The content analysis and the panel data analysis were used to investigate the cause and the effect relationship of corporate governance on the company's performance. The results indicated that there is a positive cause and effect relationship for gender diversity on the market value of industrial companies listed on the Palestinian stock exchange market. Meanwhile, corporate governance dimensions were all insignificant to the market value of investment companies listed in the Palestinian stock exchange market. Thus, corporate governance has no effect on the market value of investment companies.

1. Introduction

The industrial sector is considered one of the most vital sectors in the economy. This is due to the backward and forward linkages that it instigates. These linkages include an expansion of a country's export and foreign direct investment (Tripathy, et al., 2021; Samara, 2017). This is why, this paper will study the impact of corporate governance on both the industrial and investment sectors.

History had demonstrated the importance of corporate governance on the company's performance, where the collapse of major corporation – such as Enron, Parmalat, World and Bank of credit and commerce international (BBBCI) and others – was related to the lack of laws and regulations that strengthen the implementation of corporate governance. As a result of these financial scandals, the relationship between corporate governance and firm's performance had attracted major interest. Thus, governments throughout the world passed effective laws and regulations to monitor the performance of companies. These new guidelines played a crucial role in strengthening both the implementation of corporate governance and risk management (Tourani-Rad and Ingley, 2010; Aboagye-Octhere et. al., 2012).

In order to improve corporate governance, the board is considered a key element in securing the protection of the firm's assets and growing it. In addition, the board will also try to maximize the return on corporate investments. Thus, the board will play the role of separating the ownership from the management problem, i.e., the board will solve the agency problem (Colombo et al., 2015; Thomsen and Conyon, 2012; Gunawan, 2019; Price et. al., 2011). In summary corporate governance determines wither the corporation is heading in the right direction and is running efficiently.

The year 1994 was the birth of the semi-independent Palestinian economy. The aim was to have strong industrial and investment sectors that will enable the Palestinian economy to grow and breakaway from the Israeli economy; unfortunately, this goal was not achieved (Samara, 2017).

The purpose of this paper is to study the effect of disclosure of corporate governance on the market value of companies listed in both the industrial and investment sectors in Palestinian stock market.

The sole purpose of the company's management is to increase the wealth of the stockholders. This is achieved through increasing the price of the stock in the stock market (Al-Bsoul, 2018). This is why we will use the market value in order to measure the performance of the companies listed in the Palestinian stock exchange market. The market value is considered of vital importance for all parties using financial reports. It also plays a major role in determining an investor's decision which is related to the price of the stock (El-Sheikh Saleh, 2014).

Our aim is to determine whether an implementation of better corporate governance will improve the market value of company's performance in both the industrial and investment sectors. In other words, corporate governance might be the solution to the struggle of industrial and investment sectors, especially where these two sectors are the largest sectors in the Palestinian stock market.

The Palestinian stock market encompasses 48 companies, where the industrial sector is the largest sector that constitutes 12 companies. Meanwhile, the investment sector includes 11 companies. Thus, both sectors form 47 percent of the Palestinian stock market.

The implementation of good governance was proven to have a positive effect on the economic growth on the Palestinian economy (Samara, 2018). In this paper our objective is to analysis whether the disclosure of better corporate governance will improve the performance of Palestinian firms in both the industrial and investment sectors, given that the code of corporate governance in Palestine was instituted in 2009. So, we will investigate whether the implementation of this code had a positive effect on the market value of targeted companies.so we will investigate the impact of corporate governance on the firm's performance. It is believed that corporate governance will enhance the performance of firms and thus promote economic growth.in other worlds, corporate governance is necessary for economic growth of any nation (Bansal and Sharma, 2016).

2. Literature Review

Several studies investigated the cause-and-effect relationship between the disclosure of corporate governance and the firm's market value. Some studies showed a positive cause-and-effect relationship between these two variables. We will start our literature review with Al-Ahdal, et al. (2020), where they studied the effect of corporate governance on the performance of non-financial companies listed in the Indian stock market and the Gulf Corporation Council (GCC) stock market. A sample of 53 firms listed in the Indian stock market and 53 firms listed in the GCC stock market were considered for the time period from 2009 to 2016. A panel data analysis was performed indicating that board accountability (BA) and audit committee (AC) have no significant effect on firm's performance measured by Return on Equity (ROE) and Tobin's Q. Furthermore, transparency and disclosure (TD) have no significant effect on firm's performance. Finally, the infrastructure for implementing corporate governance is better in India compared to GCC countries.

Bubbico et al. (2012) studied the relationship between corporate governance and the market value of financial companies listed in Italian stock exchange. A cross sectional data covering the year 2010 was used to investigate this relationship. The paper concluded that there was a positive and statistically significant relationship between corporate governance and firm's performance, i.e., corporate governance implementation increases value creation for a particular firm.

Bajaher, (2020) studied the impact of corporate governance on cement companies listed in Saudi stock market. The data covered the period from 2012 – 2016. The ordinary list Square (OLS) method was used to study the impact of corporate governance on firms' performance. The results showed that managerial ownership and firm size have a significant positive impact on firm performance. Nevertheless, board independence, board size, board meeting and audit type have been not significant on the financial performance.

Pasaribu, (2017) studied the relationship between the firm performance and gender directors. The study sample constituted all of the non-financial listed firms at the UK from (2004-2012). The results showed that female directors own a positive relationship with the firm performance. The positive impact of female directors is stronger in small firms, because of large firms, which are associated with strong governance, and encounter over-monitoring problems after appointing female directors. In addition, large firms encounter greater external intervention than small firms when it comes to the composition of their boards of directors.

Memon et al., (2019) investigated the effect of corporate governance on the firm leverage. In addition, the paper studied the moderating task of firm age on the relation between leverage and corporate governance. a sample from the listed firms in China. The results showed that CEO duality and the board of directors as corporate governance dimensions with a significant effect on leverage. As board size and independence of board affect leverage positively, the firm's age affects leverage negatively.

Falah (2017) studied the relationship between corporate governance and the firm's performance in the Palestinian exchange. The data covered the period from 2008 to 2016 for a sample of 32 companies. The study utilized both correlation and Ordinary Least Square (OLS) method. The results of the paper indicated that there is a negative correlation between the board size and the firm's performance. Meanwhile, the independent directors had a positive effect on the firm's performance.

Abu Eid (2021) examined the relationship between corporate governance and the firm's performance for companies listed in the Palestinian stock exchange. The data was collected from the companies' annual financial reports and the Palestinian stock exchange for a sample of 32 companies covering the years 2006, 2008 and 2017. The study used questionnaire, and fixed and random effect model. The results showed that there was negligible relationship between corporate governance and the firm's performance. Nevertheless, when financial leverage and total asset where controlled, the model indicated that there was a positive significant relationship between corporate governance and firm's performance.

Mansur (2018) looked at the effect of corporate governance on performance of companies in Amman stock exchange. The study used descriptive literature from both western and Jordanian scholars. The study results indicated that the ownership structure had the most effect on company's performance, where institution ownership had better effect on the company's performance compared to family ownership. Finally, the study concluded that better implementation of corporate governance will improve the company's performance listed in Amman stock exchange market.

Surki (2021) the effect of corporate governance on the market value of industrial companies listed in the Palestinian stock exchange market. The study collected data for 12 firms covering the period from 2015 to 2019. The paper utilized content analysis and econometrics models. The pooled effect model was used to test the panel data analysis, meanwhile the multiple regression model was used to test the hypotheses. The study concluded no significant effect of corporate governance on firm's performance.

This paper will examine the effect of corporate governance on market value of industrial and investment companies listed in the Palestinian stock exchange market. After reviewing the above literature, we notice that the impact of corporate governance one company's performance differs from one country to another. This is due to the dominant governance system of each country. Our paper will differ from Surki (2021) in the manner in which corporate governance is measured. In addition, we will consider the time period from 2013 to 2019.

3. Methodology

3.1. Purpose of the Research

This study will adopt the panel data analysis for the annual reports of companies in both the industrial and investment sectors listed in the Palestinian stock exchange market. We will study the cause-and-effect relationship between corporate governance and the market value of the companies.

The analysis will start with the unit root test in order to determine the stationarity of the data. The Liven, Line and Chu (LLC) test will be used to examine the following null and alternative hypotheses (Lutz, et. al., 2020).

Ho: the variable has a unit root

Ha: the variable has no unit root

We will test the hypotheses at the 5 percent significant level, i.e., alpha is equal to 0.05.

Chow test and Hausman test will be utilized in order to determine the most suitable model for the panel data. The following three models are usually considered when analyzing such data: (Lutz, et. al., 2020).

1. Pooled regression or common effect model
2. Fixed effect model
3. Random effect model

3.2 Data Sources

The secondary data sources will be used in this study. More specifically, the data on the dependent variable (market value), independent variables (the board members are all independent and do not have executive positions, disclosure and transparency, and gender diversity), and control variables are capital and earning per share (EPS). The data covered the time period from 2013 to 2019. This period was chosen due to the fact that the corporate code governance was fully implemented in 2009 in Palestine. So, we allowed a lag period of four years to give firms the necessary timeframe to absorb and execute the corporate governance standard.

3.3. Population

Since the main objective of this study is to examine the impact of corporate governance on the market value of both industrial and investment firms listed in the Palestinian stock exchange market. The industrial sector was represented by 12 firms while the investment sector by 11 firms.

3.4. Variables and Their Measurement

Three types of variables will be used. First, the dependent variable is the market value – this variable is measured by multiplying the price of the stock on December 31st times the number of stocks. Second, independent variables are the board members (all independent and do not have executive positions, disclosure and transparency, and gender diversity). Third, control variables are the capital and earning per share (EPS).

Table 1: Variables and Their Measurement

Variable Measurement	
Dependent variables	
Market value	Price of stock on December 31st * No. of stocks.
Independent variables	
Board members[1]	If at least one board member is independent, then the dummy variable is one; otherwise, zero.
Gender diversity	If at least one woman is a board member, then the dummy variable is one; otherwise, zero.
Independent and experience of the auditing committee member	If at least one of the members is independent and have experience, then the dummy variable is one; otherwise, zero.
Disclosure and transparency	If there is disclosure and transparency, then the dummy variable is one; otherwise, zero.
Experience diversity	Standard deviation of board members' years of experience.
Independence diversity	Percentage of independent members to total members.
Control variables	
Capital	From the companies' annual financial reports
Earnings per share	From the companies' annual financial reports

Note:
[1] Board members are all independent and do not have executive positions, disclosure and transparency, and gender diversity

The different types of variables and their measurement are explained in Table 1.

4.Results

The Eviews10 software is used to run our statistical analysis. We will start with descriptive analysis for the variables for both the industrial and investment sectors as shown in Table 2 below.

Looking at Table 2, the mean for capital of the industrial sector is USD 10,728,584. while the mean for capital of the investment sector is USD 5,497,620. This shows that the mean of the investment sector is approximately half of the main of the industry sector.

Interestingly, the mean for earning per share of the industrial sector is 0.72 while the mean for the investment sector is 0.04. These numbers indicate that the return on the industry sector is higher than the investment sector.

Finally, the mean of the market value for the industrial sector is USD 23,694,392.00, which is lower than the mean of the market value for the investment sector that is USD 78,596,970.00.

Now we will conduct the unit root test for each of the variables to determine whether the variables are stationary overtime. The flowing results are shown in Table 3 below.

At the 5 percent significant level, there is no unit root test in any of the variables. Thus, the variables are stationary.

The following models will be used to investigate the cause-and-effect relationship of corporate governance on the market value of both the industrial and investment firms.

Industrial Model: Ln (MVInd)it = β0 + β1Capitalit + β2EPSit + β3DIit+ β4DEit+ β5DCit+ β6DGit + εit

Investment Model: Ln (MVInv)it = β0 + β1Capitalit + β2EPSit + β3DIit+ β4DEit+ β5DCit+ β6DGit + εit

Ln (MV): Natural log for market value

Capital: The company's capital

EPS: Earning per share

Table 2: Descriptive Statistics of the Variables

	Industrial Sector			**Investment Sector**		
	Capital	**Market value**	**EPS**	**Capital**	**Market value**	**EPS**
Mean	10728584	23694392	0.72	54976203	78596970	0.04
Median	9742800	22620003	0.17	18750000	33801544	0.03
Maximum Value	21180000	78060262	2.41	250000000	443000000	0.28
Minimum value	988400	450925	-0.44	4409558	3557351	-0.18
Standard deviation	6945984	18680710	3.49	75088656	126000000	0.10

Table 3 Stationary/ Not Stationary

Industrial			Investment		
Variable	**P-Value**	**Result**	**Variable**	**P-Value**	**Result**
Capital	0.0144	Stationary	Capital	0.0001	Stationary
Market value	0.0002	Stationary	Market value	0.0000	Stationary
EPS	0.0000	Stationary	EPS	0.0000	Stationary

Now we will run the Chow and Hausman test to determine which is the most suitable model for the panel data.

Table 4: Results of Chow and Hausman Test

	Test	P-Value	Results
Industrial Sector	**Chow**	**0.6679**	**Pooled regression**
	Hausman	**0.000**	**Fixed effect**
Investment Sector	**Chow**	**0.9646**	**pooled regression**
	Hausman	**0.000**	**Fixed effect**

The results from table 4 shows that the pooled regression is the most suitable model for the panel data.

Table 7: Results of Pooled Regression for industrial Sector

Independent Variables	**Coefficient**	**P- Value**	**Results**
	0.000	15.04373	Consent
Significant	0.000	1.32E-07	Capital
Significant	0.1158	0.041063	EPS
significant	0.0001	0.823595	DI
No significant	0.2428	0.298847	DE
No significant	0.3566	0.216485	DC
Significant	0.0232*	0.484524	DG
	0.597		R- Squared
	0.000		Prob (F-statistic)

At 5% significant level, alpha = 0.05

If P-Value > 0.05 then the variable is not significant

If P-Value < 0.05 then the variable is significant

Looking at Table 7, the model has an R2 of 0.597. This means that 59 percent of the variations in the market value is explained by the model. Thus, 59 percent of the variation of the market value is explained by the variation in the earning per share, capital, and gender diversity. This result adds to the literature that gender diversity improves the performance of companies as found by Khan and Abdul Subhan (2019), Lafuente and Vaillant (2019), and Xie et al. (2020).

Table 8: Results of Pooled Regression for investment Sector

Independent Variables	**P- Value**	**Coefficient**	**Results**
Consent	**0.00000**	**15.78373**	
Capital	**0.00000**	**1.58E-08**	**Significant**
EPS	**0.00120**	**3.183738**	**Significant**
DI	**0.07260**	**0.377727**	**No significant**
DE	**0.19080**	**0.286421**	**No significant**
DC	**0.09880**	**0.455764**	**No significant**
DG	**0.79260**	**0.053718**	**No significant**
R- Squared		**0.821**	
Prob (F-statistic)		**0.0000**	

At 5% significant level, alpha = 0.05

If P-Value > 0.05 then the variable is not significant

If P-Value < 0.05 then the variable is significant

Looking at Table 8, the model has an R^2 of 0.82. This means that 82 percent of the variations in the market value is explained by the model. Thus, 82 percent of the variation of the market value is explained by the variation in the earning per share and capital.

5.Conclusion

Our study had aimed to examine the cause-and-effect relationship between corporate governance and the market value of both the industrial and investment sectors. The panel data analysis indicated that there was a positive cause-and-effect relationship between gender diversity and the market value of industrial companies listed in the Palestinian stock exchange market. This result is due to the fact that having at least one woman on the board structure of the company will introduce different perspective and vision. In addition, new and creative ways will be adopted to solve a particular problem. In other words, having a woman as a board member will introduce innovational solution to problems and improve the company's performance. This result matches the finding of Musa et al. (2020) and Xie et al. (2020).

On the other hand, we noticed that the board members are all independent and do not have executive positions, independence experience of auditing committee and disclosure and transparency do not have any effect on the firm's market value. This finding agrees with Surki (2021).

This paper also indicated that there was no cause-and-effect relationship between corporate governance and the market value of investment companies listed in the Palestinian stock exchange market. This result can be explained by the simple fact that investment sector, similar to the banking sector, abide by corporate governance principles upon their establishment.

Our results- corporate governance has no effect on firms' performance – can be explained by the that the corporate cod of the corporate governance which was adopted in (2009) is taken from Organization for Economic Co-operation and Development. Even- though it is believed that these codes were altered to fit the Palestinian case, but in reality, the alteration proses was not successful in taken into account the social and culture. this can be demonstrated in the ownership system of the industry sector. most of the industry firms in Palestine are family businesses. The implementation of corporate did not have any impact in changing the ownership structure of these businesses. There for, we can say that the board structure does not relay believe that the implementation of corporate governance code will lead to better returns on their investment. Thus, the adaptation of this code is superficial and just to meet to standards imposed by the Palestinian government

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