Chapter 11
Corporate Governance and Company Performance:
A Comparative Analysisi Across Sectors in Portugal

Eleonora Santos
https://orcid.org/0000-0003-4693-0804
Centre of Applied Research in Management and Economics (CARME), Portugal

Jacinta Moreira
ESTG, Instituto Politécnico de Leiria, Portugal

Neuza Ribeiro
https://orcid.org/0000-0002-1228-2522
Centre of Applied Research in Management and Economics (CARME), Portugal

ABSTRACT

The assessment of the implementation of the corporate governance practices is important because it contributes to the efficient use of resources and, thus, increases corporate performance. However, the practice of CG in Portugal is below European standards due to several issues related to weak legal protection, concentrated ownership structures, and limited information transparency. Using a panel data of 17 firms listed on PSI20, this chapter investigates the impact of the internal CG mechanisms on corporate performance, in 2014-2018. Results show that the size of the audit committee impacts positively on firm performance. However, the number of independent members of audit committee decreases corporate performance in firms operating in services, and ownership of related parties increases corporate performance. Also, fewer leveraged firms are likely to exhibit better performances. This research provides understanding of the relationships between internal mechanisms of CG and corporate performance by comparing results across groups of sectors.

DOI: 10.4018/978-1-7998-7596-3.ch011

INTRODUCTION

The main objective of firms is to maximize their value, which depends on their organizational structure. However, when there is separation of ownership and control of a large company, agency problems arise (see for example, Fama, 1980; Fama & Jensen, 1983; Morck & Yeung, 2003; Abatino & Dari-Mattiacci, 2020; Li et al., 2020) and risk sharing between principals (owners) and agents (other stakeholders) (Abe et al., 2020; Zaid et al., 2020).

The main source of this problem is asymmetric information, enabling managers to acquire an advantage over shareholders in accessing information (Boone et al., 2019) and, therefore, being able to take advantage of the flexibility of accounting principles and rules for the disclosure of results. In particular, managers of listed companies may attempt to increase their salaries and bonuses at the expense of shareholders profit has been subject to discussion in the literature (Crossan, 2011). This problem entails an agency cost for the principal, which, if not properly restricted, can affect the potential for value creation and compromise the company's sustainability (Nuber et al., 2020).

Since corporate finance focuses on maximizing value in the decision-making process, resolving the agency's problems involves adopting incentive policies and aligning interests (for example, remuneration, indebtedness and profit sharing) (Borah et al., 2020; Carlson & Bussin, 2020). However, the development of the capital markets has motivated a strong debate about the structure and control of listed companies. Additionally, the financial scandals of some international companies have raised Corporate Governance (CG) issues, namely with regard to accountability, business with related parties and composition and functioning of the management body, the audit committee and the role of the board in the performance of listed companies (Soltani & Maupetit, 2015; Resende, 2017).Thus, there is a need to study the extent to which CG systems fulfill their role in corporate management. In this context, some studies show that the sensitivity between certain control mechanisms (for example, indebtedness and remuneration policies) and corporate performance depends on the type of majority shareholder (Unite et al., 2008). On the other hand, in countries where the labor market is poorly developed and with a high concentration of ownership, as is the case in Portugal, a greater number of non-executive directors on the board of directors would motivate the alignment of interests (Azevedo, 2013). However, because no CG system is perfect, agency problems are not solved solely by defining ownership and the administrative structure typical of each CG paradigm (Schulze et al., 2001; Dalton et al., 2003).

Therefore, the analysis of the impact of internal CG mechanisms on corporate performance is crucial in the context of agency problems.

CG is the system that controls and manages the company's activities and is composed of people, policies and processes necessary to achieve shareholders' expectations with integrity, respect, transparency and responsibility (Dewi, 2020). The purpose of the CG is, therefore, that companies be managed and managed for the benefit of all shareholders and not just in the interests of some.

CG can be considered a model that favors an environment of trust by giving the board of directors the mission of protecting the interests of shareholders and, at the same time, maximizing the value of companies (Crowther & Sefi, 2011), balancing the relationships between management and shareholders (Santos, 2009).

Good CG practices require reconciliation of CG mechanisms to minimize agency costs and allow for an efficient allocation of resources (Lal, 2019). As a result, companies with a higher level of adoption of the best CG practices have greater value creation (Danoshana & Ravivathani, 2019; Mertzanis et al., 2019). The high requirements and standards imposed by international markets oblige listed companies

Related Content