# Chapter 12
# Corporate Governance Mechanisms and Firm Performance in a Young Stock Exchange:
## The Case of I&M Bank, Rwanda

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## ABSTRACT

*This chapter aimed at assessing the contribution of a bank's listing to its governance and performance. Using a single case study, it collected data on bank governance, performance, and stability over the period 2009-18. Findings show that listing improved I&M Bank's internal governance in particular soon after it listed on the Rwanda Stock Exchange in 2008. Its board's independence, size, and ownership showed significant changes soon after it listed and listing improved its performance as well as stability through governance. A change in both the board's size and independence significantly reduced the bank's non-performing loans and increased the bank's resilience (Z-score) and lending.*

## INTRODUCTION

With a case of a young stock market in a developing country context, this study contributes to the debate on corporate governance by exploring how listing either constrains or improves the corporate governance mechanisms, as well as their effects on a firm's performance. The chapter sheds light on the changes happening in the governance and performance of a bank during its earlier stages of listing. By focusing on a specific case of a bank in Rwanda, the chapter understands how corporate governance mechanisms

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change with listing requirements on a young stock market. I&M Bank listed on the stock exchange which too is in its infancy in Rwanda. Therefore, the bank did not have any benchmark in the country. All financial institutions must comply with the external corporate governance policy imposed by the Central Bank. However, a successful listing requires additional governance policies specific to the listing process. Therefore, a listing firm has more pressure from the stock exchange if it wants to list. Coping with external pressures of complying with the Central Bank's policies and internal pressures to meet stock market governance requirements may bring changes in internal corporate governance mechanisms leading to an impact on a firm's performance and stability. This paper focuses on changes in corporate governance mechanisms as a result of complying with listing requirements.

It is known that firms, banks, and countries adopt corporate governance mechanisms in response to pressures from international markets and inter-governmental organizations, mostly channeled through reforms imposed by the World Bank (Adu-Amoah, Tsamenyi & Mensah Onumah, 2008; Chanda, Burton & Dunne, 2017; Kun Liew, 2008; Jain, Aguilera & Jamali, 2017). Therefore, banks establish and improve their governance mechanisms as a response to external pressures. Further, in developing countries, extant corporate mechanisms are imposed by different bodies which were adopted from western governance systems for improving the working environment of local firms and regulators (Tsamenyi & Uddin, 2008). It is also known that for a young stock market, listing firms must comply with certain corporate governance mechanisms established by the stock market. For the sake of staying on the stock market, newly listed firms make more efforts to comply with the stock market's corporate governance requirements. In such a situation instead of responding to external pressures to comply with certain corporate governance mechanisms, firms try and improve their corporate governance mechanisms to be accepted on a stock market and for continuing to operate on the stock market. These corporate governance mechanisms are not only external to a firm's usual practices but are also new to both the country and the firm since the stock market is new in the countery, Rwanda. This is problematic because literature shows that corporate governance mechanisms are normally embedded within a country's social-political system (Alawattage & Wickramasinghe, 2008; Mahadeo, Soobaroyen & Hanuman, 2012). Moreover, less developed countries operate under structural conditions which are very different from those in developed countries, the way things like power relationships and intra-organizational power are treated when it comes to corporate governance in countries like Ghana (Gesiye Angaye & Gwilliam, 2008) and Egypt (Kamal Hassan, 2008). It is also known that corporate governance mechanisms in developing countries with their weak judicial systems and enforcement in capital markets, expectedly lead to the adopted governance mechanisms not working (Tsamenyi & Uddin, 2008). This is also connected with ownership being concentrated in families and family linkages with external economic, social, and political actors.

However, little is known about how compliance with corporate governance guidelines affects a firm's performance. Existing literature focuses on well-established stock markets and not on newly listed firms.

Before joining a stock market, a firm has to follow corporate mechanisms imposed by the Central Bank. However, after a firm joins a stock market, more mechanisms are added, and it is in a firm's interests to comply with both the Central Bank and the stock market's regulations. What is missing is the evaluation of the effect that complying with corporate governance has on a firm's performance and whether there is an improvement, a deterioration, or a stagnation in a firm's performance due to these governance mechanisms. In other words, does listing improve internal governance and/or a firm's performance? How does improving internal governance affect the performance of a recently listed firm? Researchers also want to know the changes happening in a firm's corporate governance mechanisms as a result of adopting listing requirements and how these changes affect a firm's stability and performance. Unfortunately,

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