Financial Gearing and Corporate Governance: Impact on the Value of Pakistani Listed Companies

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Abstract
This research aims to check out the impact of corporate governance and financial leverage on Pakistan's textile firm's value. A sample of 15 textile companies is selected, out of 180 textile firms listed on PSE data from 2015 to 2019. Overall correlation results show a negative relationship between corporate governance and textile firms in Pakistan but positively correlated with financial leverage. But the regression analysis Audit committee and ROA have an insignificant impact on the firm's value and show board size negative and negligible impact on firm value. However, on the other hand, financial leverage has a positive and significant relationship with textile firms. Other findings also show board size has a negative impact on the value of Pakistan's textile firms. Finally, it is concluded that an organization with very strong management and good governance should be very good in its value. This research contributes to the literature on the affairs that effect the value of the firm. The outcome of this research possibly helps full for investors, Managers, and financial administration advisor.
Keywords: Return on Total Assets, Firm size, Financial Leverage, Board of Directors, Tobin Q

Corporate governance is concerned with the instruments or structure used to reserve an organization's stakeholders' rights stakeholders' rights. (Khatab, Masood, Zaman, Saleem, and Saeed, 2011) Describes corporate governance as the set of procedures, policies, and institutions that influence an organization's management and provides ways to control or properly manage it. Corporate governance and financial leverage are the necessary components that can answer the questions related to shareholders' wealth maximization. Corporate governance is a highly important practice because it considers the welfare of shareholders; it also includes the rights of internal and external stakeholders, like directors and investors, etc. Corporate governance also helps increase the company's goodwill because it focuses on the firm's internal control that eliminates the frauds and minimizes errors (Tahir, Rehman, & Rehman, 2014). The need for corporate governance is arising due to the following reasons.

The scandals of companies that happened in 2001, 2002, for example, World Com, Enron have decreed the speculators' certainty and make it problematic for organizations to increase the equity finance from the share markets (Agrawal, 2005).In response to these embarrassing scandals, investors think companies are not adequately managed by the board of directors and its committees. Like Enron, manipulated the financial statements. Subsequently, the board could not reveal it because the board was not independent of its senior Executives. As the World shows the high profits by manipulation, the world com filed for bankruptcy due to this scandal. The results of the investigation demonstrated that the auditors do not adequately check the duties of managers. These misshapen increases the importance of corporate governance. One of the most important corporate governance objectives that cannot be ignored is to maximize the wealth of shareholders. Shareholders' wealth can be effectively measured through the firm's market value, maximization of shareholders' wealth, the significant role played by corporate governance, and financial leverage.

If an organization wants to increase its market value, it is compulsory to make a balanced capital structure (equity debt) and follow comprehensive corporate governance (Kajola, 2008).

An increase in the leverage also increases the value of the firm. Still, up to a certain level after that, it starts declining, the cost of capital also increases due to increased leverage after the safety zone. A balanced capital structure consists of some portion of debt but not a hundred percent. (Gill & Mathur, 2011a). A study was conducted to see the association between corporate governance and an organization's operational performance in a dynamic situation of Siri Lanka (Heenetigala & Armstrong, 2012). They stated that the firm's profitability and market performance significantly increased if firms apply corporate governance codes.

Problem statement

The present paper is conducted to see the effect of firm control mechanism & financial leverage upon organization value. The answer to the above question is in both positive and negative sense. The appropriate response to the above problem can be in both senses, either positive or might be negative. Each shareholder and finance provider want to get the most extreme return against their money.

I tried to check how corporate represents impact the firm Profitability and change it working the five-year period. This research is a blend of the effect of the company's control and financial leverage on the firm's value of Textile & chemical divisions because minimal research has been directly conducted. No one provides a comparison of two sectors; the other reason is to know how the organizations can increase the stockholders and other finance providers' wealth through the productive use of the

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business resources. I have tried to give the guideline on how the burden of debt makes the negative or positive image in both ways, on the minds of stockholders and finance provider's wealth.

Hypotheses

H1: There is a positive association between Board Size and firm value

H2: There is a positive association between CEO Duality and the value of the firms.

H3: There is a positive association between the Audit Committee and the firm's value

H4: There is a positive association between Financial Leverage and Firm value.

Review of Literature

Corporate governance is a necessary component that improves the value and goodwill of an organization. Corporate governance is a subjective approach that means it varies from nation to nation. The structure of financial leverage is also not the same for every organization. It depends on the regulations of countries and the nature of business.

The majority of previous studies were conducted to see the effect of firm size on its profitability. The results of those studies revealed that the size of the firm was positively associated with its performance. In connection to this, Vijayakumar and Tamizhselvan (2010) also found the same results on the sample of 15 South Indian firms. To test the association between firm size and profitability, they used proxy variables (sales and total assets) to measure the firm's size & (profit Return on investments) to measure profitability by applying the appropriate model. The portion of the firm size that plays a significant part in generating the profitability was studied by (Lee, 2009) who have been measured through applying panel data of a sample of more than seven thousand US listed firms. He concludes that the absolute size of firm plays an outstanding role in generating the profitability.

A study based on board size and performance of banks conducted by Olubukunula and Samuel (2012) by applying the simple regression model. The results of their study stated that the banking sector's performance is negatively related to its board. they related it to the agency cost, means agency cost backed by the large size of the board. As the size of the board increases, the probability of increasing the agency cost also increases.

Becker et al. (2010) found a significantly negative association among ROA, ROE, and employees of the firm and its productivity by applying the USA public limited companies' regression model from 1987 to 2002. Whereas the study (Limpaphayom & Connelly, 2006) shows no significant relationship between firm performance and firm size.

Sheikh and Wang (2012) Most of the decision-making powers are in the hand of BOD. BOD's goal is to provide guidance for confirming the good performance and maximize the worth of shareholders. It is the responsibility of the board to lead and control the other management.

Jensen and Meckling (1976) Stated that the agency problem could be reduced by making the board lead by independent directors because independent directors critically examine the adaptable behavior of directors and control it. Findings of past studies like (Dehaene, De Vuyst, & Ooghe, 2001) (Omar, 2003) show the inconsistency between a firm's board and its performance. There would be less chance of fraud if the independent directors were more significant in number than dependent directors stated by (Uzun, 2004).

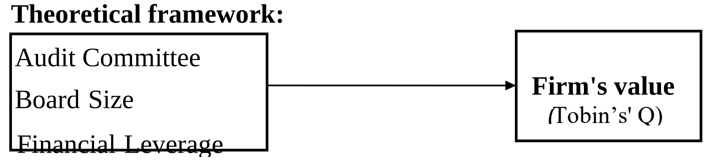
Rhodes (2000) Sated that Non-executive directors have an optimistic association with the performance of firm. For example, the researcher like (Krivogorsky, 2006) also establishes the similar results. Hasnah,(2009) Stated that NED has a significant impact on ROA.

Opposite to this revealed by (Coles, McWilliams, & Sen, 2001), he stated that the firm's performance is negatively affected by its non-executive directors. Erickson J, Park, Reising, and Shin (2005) Also found a negative impact of the board, which was dominated by independent directors on firm value. But, (De.Andres, Azofra, & Lopez, 2005)indicated no substantial connection, either positive or negative, between the firm's value and its board of directors.

Whereas, (Chan & Li, 2008) found that low performance is interrelated with the Boards that are large for members. The firm's performance and size have no significant relationship stated by (Limpaphayom & Connelly, 2006). Velnampy (2006) researched the association between the firms' economic situation and profitability by applying the Altman Original Bankruptcy Forecasting Model on twenty-five Sri Lankan firms. He concludes that only four companies out of twenty-five companies were under threat of insolvency. He also mentions that companies should use the most appropriate ratios to measure the financial leverage. Like sales to total assets, earnings/total assets ratio, etc.

Considering previous studies' results, the present study examines the impact of the audit committee on the value of firm. A strong audit committee can make the proper control over the management of an organization if the audit committee works according to CG codes. It can reduce the agency problem. Corporate governance provides the code related to the board's committees, such as the audit committee. JSC (2009) Specifies that the members of the audit committee must know accounting and finance. It also has a certificate on it. He also says that internal audit committees should meet with external auditors at least once.

Theoretical framework:



Firm size and Returns on assets have been considered as Control Variables

The dimension of Variables and Short form

The formulation and abbreviations for the dimension of all the variables are untaken in the following table.

Table 1: Dimension of Variables and Abbreviation

Variable	**Dimension**	**Abb.**
Tobin Q	The market value of Equity Book value of debt (Long term + Short term) / Total assets	Q
Size of Board	calculated as the total number of directors serve on board	BS
Audit Team	Measured as the total number of audit committee members	AC
Financial Leverage	Calculate by Total liabilities / Total assets	FL

Size of Firm	Measured through natural logarithm of total assets	FS
Return on Assets	Calculated by Net income/Total Assets	ROA

Model Specification

The following are the best suitable variables selected by me to see the consequence of corporate control management and financial leverage on firms' profitability, and the equation to investigate the association between dependent and independent variables.

Q = α + β1ROAit + β2BSit + β3ACit + β4Flit+ β5FSit + µit

Where

β_o =Constant

β1= Return on Assets

β_2= Board Size

β_3= Audit Committee

β_4= Financial Leverage

β_5= Size of firm

ε= ε is error term

Q= Tobin Q

Research Methodology

There is a total of 35 listed sectors in the Pakistan Stock Exchange (PSE). For this research, I have selected the Textile industry in this sector companies are listed. My Target Population is Textile and sector companies. Populations, as mention above, consist of Textile sector companies. I have selected 15 companies as a sample size. And the data were covering five years from 2015-2019. Data were consumed to measure the effect of the Corporate Control and financial leverage on profitability.

Linear regression and correlation models were used for this study. This technique is used to measure the impact of independent variables on the dependent variable. The data has been taken from the state bank of Pakistan and the annual reports of sample companies. The present research consists of panel data of textile firms listed on PSE (Pakistan Stock Exchange) for five years 2015-2019.

Findings and analysis

Table 2 below presented the summarization of descriptive statistics of the dependent and independent variables studied in the regression model. This table consists of mean, maximum, and minimum values and their respective standard errors. It represents the financial and non-financial variables of the fifteen textile companies of Pakistan for five years 2015-2019.

Table 2: Descriptive Statistics

	TQ	ROA	BS	AC	FL	FS
Mean	414.671	5.750	7.57	3.00	1.179	4.999
Maximum	3046.660	319.53	10	4	11.879	7.882
Minimum	15.912	-164.3	6.	2	.0066	0.000
Std. Dev.	568.155	42.560	.857	.368	2.250	2.573

The descriptive statistic shows the results of the primary dependent variable (Tobin Q), Independent variables (Audit committee, Board size, and Financial Leverage of sample firms), and the control variables (ROA and Firm size). The dependent variable Tobin Q is used to measure the Financial Performance and the Market Value of the Firm. Table 2 shows the average of Tobin Q is 414.671, and the minimum and maximum values are 15.912 and 3046.660, respectively. The mean independent variable ROA is about 5.750, and the maximum value is 319.53, and the minimum value is -164.31. The mean of BS is 7.57, and the maximum director in the board is ten, and the minimum is 6 in the textile firms. The maximum member of the audit firm is four, and the minimum is three, and the average members are 3. The above table shows the maximum value of FL is 11.879, while the minimum value is .0066, and the average value is 1. 179. Table 1 shows the mean of the textile sector's firm size is 4.999, while the minimum and maximum values are 0.000 and 7.882, respectively.

Table 2: Correlation Analysis

	TQ	ROA	BS	AC	FL	FS
TQ	1					
ROA	.297**	1				
BS	-0.078	0.045	1			
AC	.292*	-0.004	0.214	1		
FL	.658**	0.067	-0.192	0.013	1	
FS	-0.321	-0.031	.379**	-0.066	-0.616	1

The purpose of using the Pearson Correlation model is to see the degree of linear association between the mentioned dependent and independent variables. And measure how these variables are connected. Tobin Q shows a positive relationship with all variables except FS and BS, while it offers a strong positive association with FL. The correlation between ROA and BS is positive but weak. BS demonstrates a positive correlation with AC and FS and shows a negative link with FL. On the other hand, Ac shows a negative association with FS and establishes a positive relation with FL. All the variables demonstrate the negative association with FS except BS that shows a strong association with FS.

Regression Analysis

The present study used the multiple regression model to analyze the data because it helps measure the effect of numerous explanatory variables on the dependent variable (Hajijubok, Abdullah, & Ahmed, 2011). It also provides the examiner's evidence of how these variables individually and collectively affect the dependent variable. It also provides the direction of the relationship between the variables.

Table 3: Regression Model

Variable	Coefficient	Std. Error	t-Statistic	Significance
C	-1042.762	485.192	-2.149	.035
ROA	3.450	1.023	3.371	.001
BS	-63.039	57.027	-1.105	.273
AC	491.031	122.603	4.005	.000
FL	187.463	24.578	7.627	.000
FS	44.851	23.179	1.935	.057
R-squared	.603			
Adjusted R sq.	.573			
F-statistic	20.628			

The above table shows the findings of the regression model for the textile sector of Pakistan. F-statistics demonstrate the overall significance of the model. In this analysis, the F statistic is about 20.628 at a significant level of 0.00, which means the model is overall good and suitable for this data. R^2 shows the strength of the relationship between explanatory and dependent variables. In this case, the value of R^2 is .603, which means there is a 60%variation independent variable that is Tobin Q explain by the explanatory variables that are (AC, BS, FL, FS, and ROA).

Manohar and Wallace, (2003) states that there is a negative relationship exist between the size of the board and its respective value. My study's findings also show the negative and insignificant relationship between board size and the value of textile sector firms. It means as it increases the member of the board, it decreases its effectiveness.

Hermalin and Michael (2003) Demonstrate that the effect of the audit committee on the textile sector's value sector value is negative and insignificant. On the other hand, Chan and Li (2008) provide the professional information that as the level of audit expertise in the member of the audit committee increases, the firm's value can also be increased. Merawati, (2015) Established the positive relationship between the audit committee and soundness of firms financial control on its profitability

This study shows the positive and significant result of financial control found by me in the present research on the value of a firm over five years on a sample of 15 textile firms.

He confirms the inference of (De Jong, 2002), who said that the effect of leverage on firms' value is more positive and significant overtime. However, his results show a negative impact. He also stated that a more substantial value of insignificant effect specifies that no authentic U-shape relationship is expected between the equity and debt. The size of firm is also positively affecting the profitability of the sample sector.

An increase in the financial leverage level would create a negative effect on the firm's size that maybe moves to the bankruptcy of the organization. According to Beiner and Dchmid (2005), further research shows the negative and, in some cases, the insignificant effect of ROA on the FS on Pakistan's textile sector. Its mean 60.3% variation in the value of Pakistan's textile organizations is due to the independent variables (Board size, Audit Committee, Financial Leverage, Firm Size, and ROA), and the 39.7% variation is due to the other unexplained variables.

Discussion and Conclusion

Several studies have been accomplished to see the association between financial leverage and corporate governance, and the firm value, the consequences of these studies are inconsistent. Some studies found the negative association like

(Faulkender & Petersen, 2006) And (Binsebergen, van, & Graham, 2010) stated that financial leverage and firm size are negatively related to each other. Other studies found a mixture of positive and negative associations (Frank & Goyal, 2009). They conclude that financial leverage had a mixed association with the firm's size by separating the data and the period in the long run.

This study was directed to empirically test the association between corporate governance measured through proxy variables (BS, AC, CD,) and financial position, measured through (ROA, FS) on the textile sector's sample firms in Pakistan.

Overall results of the regression model show the negative correlation of Firm size, with textile firms' value in Pakistan. On the other hand, financial leverage positively correlated with the value of textile firms in Pakistan. Result also shows that ROA and Audit committee also has a positive and significant association with the value of textile companies and other finding shows that Board size was negatively correlated with the value of firm.

In conclusion, as already supposed in hypothesis one positive relationship of board size with firm value and the analysis also showed the positive and significant association between board size and firm value, which confirms the findings of previous studies. As Sanda et al., (2003) verify, that board incorporated with large members has a positive association with its profitability. Mak and Kusnadi, 2005 Also show a positive relationship with a small board incorporated with fewer members. This was done by applying the regression analysis on the sample firms. As a researcher in the third hypothesis, it is founded that there is an insignificant negative relationship between the firm's value and the audit committee. This result does not match previous research, as Chan and Li (2008) stated that a higher level of expertise in the audit committee member increases a firm's value. My results were consistent with these findings.

And in the result was shown that financial leverage generates a significant positive association among firm value. Cheng and Tzeng (2011) researched Taiwan listed companies and found a positive association between leverage and firm value.

So, last I concluded that all the variables positively affect the firm's profitability except the size of firm.

Limitations

- ❖The limitations of the present study are related to its sample size, which consists of only 15 companies in the textile sector
- ❖This study is just limited to one sector, which is the textile sector.

Future Research and Recommendations

Further study might be possible by including more corporate governance determinants like a Board meeting, Board composition, Family ownership structure, and the sample size increase. This may consist of a combination of other sectors. It also can include women's role inboard and on firm value.

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