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Effects of Corporate Governance on Financial Performance of Commercial Banks in Rwanda. Case of Bank of Kigali

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ABSTRACT

This article explores the impact of corporate governance, specifically transparency and disclosure, board of directors, and internal controls, on the financial performance of commercial banks, focusing on Bank of Kigali in Rwanda. By surveying 284 participants from management and audit departments, the study examines how transparency and disclosure practices are perceived to affect financial performance. The results show a generally positive perception, with a mean score of 4.89 for financial statements prepared according to recognized accounting standards. In addition, there is a noted concern about finding the right balance between transparency and confidentiality (mean score 2.02). In terms of the influence of the board of directors, respondents strongly believe in their ability to impact financial performance, with a mean score of 4.56. Effective boards are seen as strategic partners driving financial success, although their influence is just one among many factors affecting performance. Likewise, internal controls are acknowledged for their positive influence, particularly in ensuring compliance (mean score 4.03). Strong internal controls contribute to risk mitigation, accurate reporting, and stakeholder trust, all of which enhance financial performance and sustainability. Statistical analyses, including regression models, reveal a significant correlation between corporate governance factors and financial performance. Transparency and disclosure, board effectiveness, and internal audit practices collectively explain a substantial portion of the variation in financial performance (adjusted R Square = 0.570). These findings highlight the importance of strong corporate governance practices in commercial banks, particularly in building trust, boosting stakeholder confidence, and driving financial success.

Keywords: *Corporate governance, transparency and disclosure, Board of Directors, Internal Controls financial performance*

INTRODUCTION

The last three decades has seen the term “corporate governance” emerged clearly as an independent field of study. Its scope has also witnessed great expansion such that it is now an amalgam of different disciplines, including accounting, economics, ethics, finance, law, management, organizational behavior, and politics, among others, with no universally accepted definition (Ntim, 2018). The Securities and Exchange Commission (SEC), the nation's market regulator, spearheaded the attempts to improve corporate governance in this setting Despite the SEC's existence since the 1930s, it took the organization forty years to start cracking down on market manipulation and boards that were "asleep at the wheel" while it was happening.

Investors and shareholders began to genuinely care more about the companies they invested in starting in the 1990s. Suddenly, everyone wanted answers on how businesses behaved and how they made internal decisions. That level of attention has continued to grow to this day. High-profile scandals throughout the world have piqued the interest of academic and professional researchers in corporate governance (Klenam & Enya, 2023). The widespread failure of major firms over many decades has led to increased interest in the subject both in developed and emerging nations (Adegbite, 2012). In the wake of previous financial crises and scandals, requests were made for stricter corporate governance policies, leading to the prominence of the issue of corporate governance (Abdullah & Tursoy, 2022).

Since corporate governance also offers the framework for achieving a company’s objectives, it encompasses practically every sphere of management, from action plans and internal controls to performance measurement and corporate disclosure (James & Margaret, 2023). Its structures and techniques are desirable to impose all parties to work together towards a common goal (stewardship theory). As such, sound corporate governance has become a critical success factor for firms (Younas, 2022) and a company’s efficient operation (Klenam & Enya, 2023). Corporate governance has become critical for strengthening firm performance, protecting investor rights, enhancing the investment climate, and stimulating economic growth (Binh & Hoang, 2020). By establishing appropriate incentives and controls, corporate governance can help reduce conflicts of interest and improve the company's financial performance by increasing the value of the company and the return on investment for shareholders (Wajdi & Anis, 2023).

This will boost public confidence and ensure efficient and effective functioning of the banking system (Aisha & Adamu, 2022). According to Oloniluyi, Akode, & Osasona (2023), banking supervision cannot function well if sound corporate governance is not in place. Consequently, banking supervisors have strong interest in ensuring that there is effective corporate governance at every banking organization. It is a control and monitoring system in which the board of directors oversees the work of management to maximize shareholder value (Hani, Rebecca, & Yahya, 2022). Corporate governance is one

of the most important dimensions of ESG (environmental, social and governance) indices revealing its capacity to ensure legitimacy (Bayelign, Ayalew, & Sitotaw, 2022), trust and the reputation of banking firms during crisis (Hani, Rebecca, & Yahya, 2022).

The issue of Corporate Governance is of much concern for the banking sector as these financial institutions are a key element in the payment system and play a major role in the functioning of economic systems both in developing as well as developed nations. In Rwanda, the problems with and requirement for corporate governance have been fueled by business scandals in nearby nations in the East African Community particularly in Kenya and Uganda, as well as globally.

So, this research is important, the researcher will be able to know how Corporate Governance affects the Financial Performance of financial firms which are banks. There is also limited literature and empirical studies that look at the phenomenon and state of corporate governance in Rwanda. Most of the available literature on corporate governance mainly focuses on developed countries and African countries such as South Africa, Nigeria and Kenya. This study had contributed to the current literature by assessing the effects of corporate governance on financial performance of commercial banks in Rwanda.

LITERATURE REVIEW

This section examines the effects of corporate governance on the financial performance of commercial banks. It entails a conceptual, theoretical, empirical review, conceptual framework and research gap.

Lawton (2023) defined corporate governance as combination of rules, processes or laws by which businesses are operated, regulated or controlled. Corporate governance essentially involves balancing the interests of a company’s many stakeholders, such as shareholders, senior management executives, customers, suppliers, financiers, the government, and the community. In order to assure the board's efficacy and efficiency and greater financial performance, the board size should be reduced. This study comes to the conclusion that a firm's performance is greatly impacted by its corporate governance structure. Therefore, the report advises that directors and other stakeholders should put in place proper governance frameworks in order to increase financial performance. Regulators and policymakers should develop rules and laws to make sure businesses have the right governance structures in order to improve performance.

Bayelign, Ayalew, & Sitotaw (2022) looked into the effect of corporate governance on the financial performance of Ethiopian insurance companies that are heavily regulated. The study used econometric panel data from nine insurance companies between 2012 and 2020 and an explanatory research design. The approach of random effect estimation was utilized to identify the most important variable. As explanatory variables, board size, managerial soundness, board remuneration, financial disclosure, debt, and dividend policy were utilized to quantify financial performance using return on assets and equity. The findings showed that while debt and dividend payout have a negative and substantial influence on insurance company financial performance, board size, managerial soundness, board remuneration, and financial disclosure have a positive and significant impact. The study shows that all corporate governance practices significantly affect the financial performance of insurance companies in Ethiopia as determined by return on assets and equity.

Al-ahdal, Alsamhi, Tabash, & Farhan (2020) analyzes the impact of corporate governance mechanisms on the financial performance of Indian and GCC listed firms. The study used a sample that consists of 53 non-financial listed companies from India and 53 non-financial listed companies from GCC countries for the period from 2009–2016. According to the findings, the audit committee and the board's accountability have little bearing on a company's success as assessed by ROE and Tobin's Q. Similar to this, TD has a negligible detrimental effect on firms' performance as indicated by Tobin's Q.

Janka & Katarína (2020) explored and compare the impact of selected financial and non-financial determinants representing the interests of these groups on corporate financial performance. The influence of determinants of CG on financial performance, measured by return on assets (ROA), return on equity (ROE) and return on sales (ROS) indicators, is investigated by means of correlation analysis. The sample of businesses used comprises of Slovakia-based banks, insurance companies, and non-financial joint-stock companies registered on the Bratislava Stock Exchange. The results demonstrated that each of the CG determinants under investigation has an impact on the financial success of businesses. The amount of total equity (EQ), the average compensation (AR), and the number of members of the Board of Supervisors (BSM) all have a major impact on the ROA, ROE, and ROS of share issuers. The only factor affecting performance measures with banks is total personal costs (PC). The dividend ratio (DR), EQ, AR, and BSM have an impact on ROA, ROE, and ROS for all companies.

Tiep, Ngo, & Tran (2021) carried out a study to understand intensively the impact of corporate governance on firm value by exploring the mediation mechanism of corporate social responsibility and organizational identification in the relationship between corporate governance and firm value. Because it is suitable for organizational and management research, like the study being undertaken here, covariance-based structural equation modeling (CB-SEM) analysis was chosen. Due to their importance, this study focused on small and medium-sized enterprises (SMEs) in emerging economies. This study makes a contribution by offering more empirical data demonstrating how crucial corporate governance is to raising firm value. Additionally, the empirical data on the mediating roles of organizational identification and corporate social responsibility in the link between corporate governance and company value is the primary focus of this work. The originality of this study is further enhanced by its applicability to the SME setting in emerging economies.

Goel (2018) explored the effectiveness of these corporate governance reforms by analyzing the corporate governance practices followed by Indian companies in two reform periods (FY 2012–13 as Period 1) and (FY 2015–16 as Period 2). Considering mandatory regulations as per clause 49 of Listing agreement with Securities exchange board of India and the governance norms in the new Company Act, 2013, corporate governance performance (CGP) index was developed to evaluate the corporate governance rating of Indian firms. Although the fundamental corporate governance structures of Indian firms have greatly improved, fewer independent directors have been recruited to the board as a result of the improvements. Following corporate governance practices has significantly improved in all the examined sectors as a result of the reforms. The integrated framework of total company social

performance and financial performance only shown a significant association during the study period. Long-term improvements in corporate governance have no effect on financial connections in the Indian economy.

Ausat, (2019) investigated the relationship of corporate governance and financial performance for Islamic Banks. By looking through the annual reports of the banks from 2013 to 2017, the Orisis database was used to gather the corporate governance variables and financial data. With a panel data technique and a set of 60 firm-year observations, the sample included 12 listed Islamic banks from various nations. To examine their impact on a firm's performance as measured by ROA and ROE, the corporate governance factors chosen included board size, CEO duality, board independence, and size of the Shariah Supervisory Board. In order to lessen the degree of external influence throughout the study, additional firm-level factors, such as the size and age of the banks, were incorporated. The data were analyzed using descriptive statistics, the Pearson Correlation Matrix, Generalized Least Squares (GLS) regression, and the Random Effect Model.

The conclude on this, one can argue that it has not conclusive on the extent to which corporate governance can have positive influence on the financial performance of banks in Rwanda.

And also, other built on the firm argument that the board size, its dependency and accountability are essential factors on the success of corporate leadership and how it influences banks' performance. It did not consider the impacts of financial firms especially in Rwanda and how internal audit and disclosure affects the firms' performance. This study strives to cover this literature gap by performing a survey on bank of Kigali.

METHODOLOGY

The research design to be used is a descriptive method as data have been gathered, collected and analyzed in a manner that is understandable to the users. Online survey tools have been used to gather data as per the research objective. A wide variety of data gathering techniques, including case studies, observational techniques, and survey approaches, may be used with this design. The sample comprises of Rwandan bank, which is among the financial firms; listed on the RSE. The researcher selected Bank of Kigali as their case study as it is among the leading banks in Rwanda with a high coverage among other banks in Rwanda. The study population consisted of 978, employees of BK headquarter mainly the employees in audit and assurance and in finance and accounting departments.

In the total population of employees 978, the researcher had taken a sample of 284 employees for bank of Kigali mainly targeting top management, audit and assurance department and the finance department. Thus, during this study, the sample size was selected using the yamen's formulas indicated below:

$$n = \frac{N}{1 + Ne^2}$$

n – Sample size

N – Population size

(e)- The margin of error (which is 0.05)

The population size is 978 representatives of employees of Bank of Kigali as follows:

$$n=\frac{978}{1+978(0.05^{2)})}$$

=284

FINDINGS

4.1 Demographic characteristics of respondents

Collecting demographic data is crucial in research because it aids in understanding the composition of the study population and identifying any potential biases that may affect the results.

4.1.1 Gender of the respondents

Table 1. Distribution of respondents by gender

Gender	Frequencies	%
Male	175	61.62%
Female	109	38.38%
Total	**284**	**100.00%**

Source: primary data

The study's gender distribution among participants was a major discovery. Around 61.62% of the total participants, or 175 people, were male, while around 38.38%, or 109 people, were female. As a result, both genders were not fairly since the number of female respondents is still low.

4.1.2 Age of the respondents

Table 2 – Distribution of respondents by age

Age of respondents	Frequencies	%
18 – 25 years	55	19.37%
26 – 35 years	109	38.38%
36 – 55 years	93	32.75%
Over 55 years	27	9.51%
Total	**284**	**100.00%**

Source: primary data

The table above reveals that 38.38%of the entire sample is between the ages of 26 and 35, showing a considerable level of participation or impact of the subject matter under investigation on this age group. Furthermore, 32.75% of respondents are between the ages of 36 and 55, indicating a substantial presence of middle-aged people in the survey. This age variety adds value to the data by gathering opinions from different life stages. The range of age groups enriches the data by providing viewpoints from diverse periods of life. It is worth mentioning that the age range of 18 to 25 years, which accounts for 19.37% of the participants, contains younger persons who may provide useful insights regarding the relevance of the research topic to the youth. In addition, respondents above the age of 55 representing 9.51% are included, indicating the views of the elder generation.

4.1.3 Education of respondents

Table 3 – Distribution of respondents by level of education

Education level	Frequencies	%
Certificate	0	0.00%
Diploma	0	0.00%
Bachelors	173	60.92%
Masters and above	111	39.08%
Total	**284**	**100.00%**

Source: Primary data

The table presents a breakdown of the participants' educational levels. The majority of the 173 responders (60.92%) hold Bachelor's degrees, indicating a considerable proportion of individuals with undergraduate education. Furthermore, 39.08% of participants had Master's degrees or higher, indicating a significant presence of people with advanced academic backgrounds. Nonetheless, it is worth noting that none of the participants possessed certificates, and diploma. This distribution emphasizes the study's participants' excellent educational achievements, with a concentration on undergraduate and postgraduate qualifications. This diverse educational background provides a helpful perspective for the research because it comprises a wide range of academic experiences and perspectives that can significantly improve the study's discoveries and overall quality of analysis.

4.1.4 Working experience of respondents

Table 4 – Distribution of respondents by working experience in organization

Working experience	Frequencies	%
Less than 1 year	18	6.34%
1 – 3 years	95	33.45%
4 – 5 years	76	26.76%
6 – 8 years	53	18.66%
9 – 10 years	27	9.51%

11 years and above	15	5.28%
Total	**284**	**100.00%**

Source: Primary data

This table depicts the distribution of respondents based on their job experience within organizations. The results show that there is a diverse representation of individuals with varying degrees of experience. The bulk of respondents (26.76%), have 4 to 5 years of experience, indicating the existence of a sizable number of mid-level professionals in the sample. Furthermore, 33.45% of participants had 1 to 3 years of experience, showing a sizable proportion of people in their early careers. A sizable proportion of seasoned professionals, 9.51% of those polled, had worked for 9 to 10 years. less than one year represented as (6.34%), 6 to 8 years (18.66%), or 11 years or more (5.28%). This distribution shows a fair representation of different career stages, which adds to the credibility and comprehensiveness of the insights gained from the study's wide group of participants.

Effects of transparency and disclosure on financial performance of commercial bank

The study has established the effects of transparency and disclosure on financial performance of Bank of Kigali measured using these 6 items scored on a five-point Likert scale ranging from: (5) for strongly agree, (4) for agree, (3) for not sure, (2) for disagree, (1) for strongly disagree. Respondents were asked to rate their level of agreement or disagreement with statements about this topic. To summarize the data collected from the participants, descriptive statistics such as averages and standard deviations were used.

Table 5 – Effect of transparency and disclosure on financial statements

Statement	N	Mean	SD
Financial statements are prepared according to recognized accounting standards	284	4.89	0.32
Audited financial statements and reports are regularly publish by BK	284	4.25	0.27
Disclosures are timely, accurate, and easily accessible?	284	3.05	0.45
The organization actively engage with stakeholders and seek their input on important decisions or initiatives	284	4.03	0.25
Information about board member qualifications, affiliations, and potential conflicts of interest are available	284	2.02	0.12
BK discloses the structure and composition of its board of directors or governing body	284	3.52	0.22

The table above provides crucial insights into the perceived effects of transparency and disclosure on financial performance of commercial bank in Rwanda based on a poll of 284 employees. The mean scores show the respondents' average judgements of effects of transparency and disclosure on financial performance, which vary from 2.02 to 4.89. The statement "The financial statements are prepared according to recognized accounting standards" obtained the highest mean score of 4.89, with a reasonably low standard deviation (SD) of 0.32. The findings show that respondents generally think that introducing transparency and disclosure has a positive influence on financial performance, suggesting enhanced Investor Trust. The statement, "Information about board member qualifications, affiliations, and potential conflicts of interest are available" obtained a lower average score of 2.02, with a relatively modest standard deviation of 0.12. According to the statistics, there is disagreement among individuals polled that a balance between transparency and confidentiality is crucial while ensuring meaningful and understandable information for stakeholders as they are also key to firm's overall success.

Using SPSS, a regression model has been conducted and following are the results. Through the calculation of their mean values, the data was merged to form variables for each factor. Following that, a Pearson Correlation analysis and a Multiple Regression Analysis were performed with a xx% confidence interval and a significance threshold of x%. The results of these analyses are presented in the sections that follow.

Table 9 - ANOVA

Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	113.502	30	3.786	3.284	.026[a]
	Residual	275.194	254	1.083		
	Total	388.776	284			

The model fit results are shown in above table as shown, the F-statistic was **3.284** and was significant **(Sig= 0.026),** this means that the Model was good enough to explain the relationship between the variables of the study.

Table 10 - Model summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.869[a]	.755	.570	.25192

a. Predictors:(constant), transparency and disclosure, board of directors, internal audit, Findings in Table 10 provide both the coefficient of determination is Adjusted R Square and the coefficient of correlation is R.

The coefficient of determination (R^2=0.570) explained the explanatory power of the model and indicates that 57.0% of variation in the level of financial performance of commercial bank especially bank of Kigali is being explained by the variation in the explanatory variable such as transparency and disclosure, board of directors and internal audit. The coefficient of correlation (R=0.869) is greater than 0.5. This indicates that there is a strong positive and moderate relationship between corporate governance and financial performance of commercial bank especially bank of Kigali.

Table 11 - Estimated coefficients of the model

Model		Unstandardized Coefficients		Standardized Coefficients		
		B	Std. Error	Beta	T	Sig.
1	(Constant)	.806	.292		2.760	.046
	Transparency and disclosure	.606	.205	.822	2.886	.044
	Board of directors	.762	.279	386	2.731	.047
	Internal audit	.652	.221	.469	2.9502	.042
a. Dependent Variable: financial performance of commercial banks						

There is a correlation between corporate governance and financial performance of commercial banks especially bank of Kigali. (b=0.606, sig=.046) indicating that Transparency and disclosure itself explain 60.6% of the variation in the effectiveness of the level of financial performance of commercial banks especially Bank of Kigali. Moreover, there is significant and strong positive relationship between Board of directors and evaluations with level of financial performance of commercial banks especially R Bank of Kigali. (b=0.762, sig=0.047) indicating that the 47.0% of the variation in the level of financial performance of commercial banks especially Bank of Kigali.is explained by Board of directors. Internal audit has significant and positive relationship with the level of financial performance of commercial banks especially Bank of Kigali. (b=0.652, sig=0.042) indicating that 42.0% of the variation in the level of financial performance of commercial banks especially Bank of Kigali. is explained by Internal audit.

CONCLUSION

The study aimed to assess how transparency, board of directors, and internal controls affect the financial performance of commercial banks. In terms of transparency and disclosure, most participants believed it has a positive impact on financial performance, with an average score of 4.89. However, there are concerns about finding a balance between transparency and confidentiality, as indicated by the mean score of 2.02. As for the board of directors, respondents widely recognized their influence on financial performance, with an average score of 4.56. The board's role in governance, strategic direction, and compliance was acknowledged. However, it's important to note that the board's impact is just one of many factors affecting financial performance. In terms of internal controls, participants acknowledged their positive impact, especially in ensuring compliance (mean score 4.03). Strong internal controls contribute to risk mitigation, accurate reporting, efficiency, and stakeholder trust, all of which enhance financial performance and sustainability. Concluding, transparency, effective boards of directors, and robust internal controls are crucial for a bank's financial success, but their impact is influenced by various internal and external factors. Balancing transparency and confidentiality, utilizing board oversight effectively, and implementing strong internal controls are essential for maintaining financial performance and stakeholder confidence

RECOMMENDATIONS

This study recommends that:

- The role of transparency should be strengthened and members should devote more time and commitment to perform their oversight functions and appointment to the bank, should take care of technical competency (qualification and experience) of the members
- The board of directors need to meet regularly, be independent to take all decisions on matters affecting their respective institutions
- The management of the bank should ensure that employees are trained and informed about their roles in maintaining internal controls

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