

**ASSESSMENT ON THE APPLICATION OF CORPORATE
GOVERNANCE PRACTICES IN THE ETHIOPIAN PRIVATE
COMMERCIAL BANKS: THE CASE OF DASHEN BANK S.C.**

**A THESIS SUBMITTED TO THE SCHOOL BUSINESS AND
ECONOMICS IN PARTIAL FULFILLMENT OF THE REQUIREMENTS
FOR THE DEGREE OF MASTER OF BUSSINESS ADMINISTRATION**

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**June, 2015
Adama**

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Declaration

I, the undersigned student, declared that this project entitled “**Assessment on the application of corporate governance principles in the Ethiopian commercial banks: The case of Dashen Bank s.c.**” is my original work. I have carried out this project work independently with the guidance and support of my project advisor. This study has not been submitted to any Degree/Diploma in any institutions, and that all sources of materials used for the study have been duly acknowledged.

Asegid Tadele
Name

Signature

June, 2015
Date

Certificate

This is to certify that **Asegid Tadele** has worked his project on the topic “**Assessment on the application of corporate governance principles in the Ethiopian commercial banks: The case of Dashen Bank s.c**” under my supervision. To my belief, this work undertaken by **Asegid Tadele** is original and qualifies for submission in partial fulfillment of the requirements for the award of Degree of Masters of Business Administration.

Solomon Alemu (PhD)

Date

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List of Acronyms

OECD: Organization for Economic Cooperation and Development

CEO: Chief executive officer

NBE: National Bank of Ethiopia

BOD: Board of directors

CCANB: Comptroller of the currency administrator of National Banks

SEBI: Security and exchange board of India

IOD: Institute of Directors

SFI: Supervision of financial institutions

ACCA: Association of chartered certified Accountants

ABSTRACT

In most countries management of corporations are legally responsible to shareholders. Vives Xavier (2000) pointed out that in practice management does not pursue the interest of shareholders instead they pursue their own interests which resulted in waste and inefficiency.

Corporate governance systems are therefore useful to set internal regulations that are in accordance with applicable law and exercising the corporate autonomy protected by such law, ensure the best accomplishment of the purpose of the Company as a large international company operating under widely differing economic and social conditions, as well as the fulfillment of the corporate interest, which is understood as the common interest of all shareholders of an independent company oriented towards the sustainable development of its corporate object and the creation of long-term value, with a significant institutional and retail shareholder base.(IBERDROLA. 2015)

This study was conducted to assess the extent to which corporate governance principles are applied in the Dashen Bank. A descriptive case study was employed to achieve the goal of this research. Four of the board members and twenty six senior managers which are a total of 30 participants were involved in the study. In order to get relevant data from the target population questionnaire and interviews were used. The questionnaire was administered to the board members and senior manager. The data collected through questionnaire were analyzed using frequency and percentage values and the qualitative data were analyzed using textual explanations. Furthermore, the qualitative data (data from interview) were analyzed together with the quantitative one to triangulate the results found from the questionnaire. The findings generally indicate that the extent of the application of the corporate governance principles in Dashen Bank is encouraging even though the bank has still a problem with regard to sufficient time of the board, concerning disclosure of material information on the website, independency of the risk committee and minority shareholders voting rights. As a result, the study presented some possible recommendations so as to alleviate the problems. These include, ensuring board members are full time employees, disclosure of information's in the website on timely fashion, making the risk committee independent and so on.

Key words: corporate governance, corporate governance principles.

CHAPTER ONE

INTRODUCTION

1.1 Background of the study

In most countries management of corporations are legally responsible to shareholders. Vives Xavier (2000) pointed out that in practice management does not pursue the interest of shareholders instead they pursue their own interests which resulted in waste and inefficiency.

Investors (the outsiders) cannot perfectly monitor managers acting on their behalf since managers (the insiders) have superior information about the performance of the company. So there is a need for certain mechanisms that prevent the insiders of a company using the profits of the firm for their own benefit rather than returning the money to the outside investors. (Jakob and Razvan. 2013)

System of rules and institutions that determine the control and direction of a company and that define relations among the company's primary participants including board of directors, managers, shareholders and other stakeholders are called corporate governance principles.(A.C Fernando. 1997)

Corporate governance systems are therefore useful to set internal regulations that are in accordance with applicable law and exercising the corporate autonomy protected by such law, ensure the best accomplishment of the purpose of the Company as a large international company operating under widely differing economic and social conditions, as well as the fulfillment of the corporate interest, which is understood as the common interest of all shareholders of an independent company oriented towards the sustainable development of its corporate object and the creation of long-term value, with a significant institutional and retail shareholder base.(IBERDROLA. 2015)

Banks serve a crucial role in the economy by intermediating funds from savers and depositors to activities that support enterprise and help drive economic growth. Banks' safety and soundness is the key to financial stability, and the manner in which they conduct their business, therefore, is central to economic health (Basel Committee for Banking Supervision, 2006).

In every system, there are major components that feature paramount for the survival of the system. This is also applicable to the financial system. The banking institution has been contributed significantly to the effectiveness of the entire financial system as they offer an efficient institutional mechanism through which resources can be mobilized and directed from less essential uses to more productive investments (Wilner, 2000).

The governance principles have gradually become the criteria with which the companies must comply in order to be competitive enough. Compliance with the principles of corporate governance is a determining factor for performing well on a permanent and consistent basis thereby help increase confidence in the company, reduce the cost of capital and induce a suitable ground for procuring long-term financing. Implementation of governance principles provide for the responsibilities of the board to set policy and strategic direction to the organization and monitoring management's performance against that shape the organizations framework for accountability, transparency, probity and respect for the rights of all stakeholders (Massie, 2000).

Agrawal (1996), pointed that better governed banks have more efficient operations and better performance due to some reasons; governance may reduce the incidence and amounts of related-parties transactions and other "self-dealing" practices, better governed banks may have lower cost of capital, especially if they employ subordinated debt financing, better governance may translate in to more efficient and streamlined operations.

Governance of banks plays a vital role Hence banks are considered as vital institutions in any economy as they form an important source for providing finance to businesses. In view of this role and of the fact that the activities of commercial banks affect the greater part of the society, these banks are selected as the main focus of this study,

Since, capital market conditions are not developed enough in Ethiopia, commercial banks play important primary role as financial intermediaries in the economic growth process, channeling funds from savers to borrowers for investment. As financial intermediaries, banks play an

important role in the operation of an economy. In such away, commercial banks are key providers of funds and their stability is of paramount importance to the financial system.

As a result well functioning of banks are important to the overall economy so an understanding of corporate governance for this matter is essential and crucial to the stability of the economy since the overall operation of the company is primarily based on smooth operation of internal environment. Accordingly, this study is an attempt to shed light on the assessment of scarcely studied area of applicability of corporate governance principles in the Ethiopian private commercial banks, the case of DB.

1.2 Statement of the Problem

Commercial banks have overtime become very important institutions in the financial system as they function as retail banking units facilitating the transfer of financial assets that are well desired from some part of the public (Fund Lenders) into other financial assets which are more widely preferred by greater part of the public (fund seekers) (Saunders, 2001).

Thus, corporate governance refers to all issues related to ownership and control of corporate property, the rights of shareholders and management, powers and responsibilities of the Board of Directors, disclosure and transparency of corporate information, the protection of interests of stakeholders that are not shareholders, enforcement of rights etc... (Fekadu, 2010),

Effective Corporate Governance practices are essential to achieving and maintaining public trust and confidence in the banking system, which are critical to the proper functioning of the banking sector and economy as a whole. As we know banking sector has been performing an essential role in strengthening any economy. Poor Corporate Governance may contribute to bank failures, which can pose significant public costs and consequences due to their potential impact on any applicable deposit insurance systems and the possibility of broader macroeconomic implications, such as contagion risk and impact on payment systems. In addition, poor Corporate Governance can lead markets to lose confidence in the ability of a bank to properly manage its assets and liabilities, including deposits, which could in turn trigger a bank run or liquidity crisis (Basel Committee for Banking Supervision, 2006).

In spite of the intrinsic importance for the economic health of corporations, economy and society in general, however, the extent to which banks are complying with or applying these principles is the least studied area of management especially in developing countries like Ethiopia the awareness on the application of corporate governance principles seems very poor. The required attentions were not given until recent times.

Up to the knowledge of the researcher although, some of earlier studies have made to add their own contribution to the principles of corporate governance in Ethiopia the researcher believes that dealing with the extent to which the corporate governance principles are implemented on Ethiopian private commercial banks (the case of Dashen Bank) is worth discussing and addressing issue.

Thus, this study aimed to contribute to the current literature by providing some evidence on the factors that contributes to the application of corporate governance principles on commercial banks in Ethiopia by taking the following research questions into account.

- Is there transparency and disclosure of material information in the bank with shareholders and stakeholders of the bank?
- Does rights of shareholders and other stakeholders protected?
- To what extent the board is discharging its roles and responsibilities?
- Do the relevant committees discharge their responsibility accordingly?

1.3 Objective of the Study

i. General objectives

The main objective of the study is to assess the extent to which the corporate governance Practices are applied in the Ethiopian private commercial banks, the case of Dashen Bank.

ii. Specific objectives

The specific objectives of the study include:

- To assess if there is transparency in the bank.
- To assess if there is disclosure of material information in the bank.
- To assess whether the rights of shareholders is protected.
- To assess the extent to which the board is discharging its responsibilities
- To study to what extent the bank guarantees the efficiency of the board
- Assessing whether the committees of the bank discharge their responsibility or not.

1.4 Scope of the Study

This study was confined only to Dashen Bank. The conceptual scope of the study was therefore, limited to examine the extent to which the corporate governance practices are applied in this bank.

1.5 Significance of the Study

The findings of this research may have certain areas of significance.

- For the Bank, the study was aimed at to examine the extent for applying the corporate governance principles and make recommendations.
- Indirectly it also can be applicable to other privet commercial banks in the country.
- The study may serve as a guide for the participants of the corporate governance like the board and senior managers to test them to what extent they are using their rights.

- And the last but not the list, the study may serve as a reference material for other researchers who need to make a research on this area.

1.6 Limitations of the Study

The researcher faced many problems as no research is free from limitations which, in fact, may affect the quality of the study. The following were among others:

- Unwillingness of respondents to fill the questionnaire
- Lack of timing to give back the questionnaire
- The study lacks access to various research literatures specifically done on the case of commercial banks in Ethiopian.

1.7 Organization of the study

Generally the study is comprised of five distinctive chapters. The first part has given the brief introduction about the study. Chapter two gives different literature reviews about corporate governance principles. Chapter three provides a brief explanation about the methodologies used for the study. In what follows, chapter four is the analysis part which assess the extent of application of corporate governance principles in private commercial banks in Ethiopia case in Dashen bank s.c and chapter five concludes and gives recommendation.

CHAPTER TWO

LITERATURE REVIEW

2.1. What is Corporate Governance?

Different authors view the meaning of corporate governance differently. For example, one school of thoughts describes corporate governance as a “system” by which companies are directed and controlled (Cadbury and Greenbury Report, 1992). But it must be kept in our mind that the fundamental concern of corporate governance is to ensure the conditions whereby a firm’s directors and managers are held accountable, ensure better and effective protection to all stakeholders. The World Bank argues that the framework of corporate governance should be based on four pillars such as Responsibility, Accountability, Fairness and Transparency.

According to Kocourek, (2003), to counter the accounting, leadership, and governance scandals, organizations are rushing to institutionalize corporate governance, which may be even be counterproductive. The drive to more tightly regulate the membership and functions of corporate boards is already encouraging companies to view governance as a legal challenge rather than a way to improve performance. There is no universally accepted code that ensures good corporate governance. But there are some variables on which the corporate governance framework established. Those are Responsibility, Accountability, Fairness and Transparency.

Corporate managers, investors, policy makers, and lawyers, on the other hand, tend to employ a narrower definition. For them, corporate governance is the system of rules and institutions that determines the control and direction of the corporation and that defines relations among the corporation’s primary participants. (Ibid)

The definition used in the United Kingdom’s 1992 Cadbury Report is widely cited from this perspective, and it reads: “Corporate governance is the system by which businesses are directed and controlled.

The OECD principles define corporate governance as involving “a set of relationships between a company’s management, its board, its shareholders, and other stakeholders. Corporate governance also provides the structure through which the objectives of the company are set, and the means of attaining those objectives and monitoring performance are determined. Good corporate governance should provide proper incentives for the board and management to pursue objectives that are in the interests of the company and its shareholders and should facilitate effective monitoring. The presence of an effective corporate governance system, within an individual company and across an economy as a whole, helps to provide a degree of confidence that is necessary for the proper functioning of a market economy.”

Magdi and Nadereh (2002) stress that corporate governance is about ensuring that the business is run well and investors receive a fair return. The corporate governance structure specifies the distribution of rights and responsibilities among different participants in the corporation such as the board, managers, shareholders and other stakeholders, and spells out the rules and procedures for making decisions on corporate affairs.

Corporate governance is the process by which a board of directors through management guides a company in fulfilling its corporate mission and protects the company’s assets over time. The board of directors on behalf of the shareholders is established with the objective of providing oversight and guidance to the managers of a company, (ibid)

Corporate governance is not just corporate management; it is something much broader to include a fair, efficient, and transparent administration to meet certain well defined objectives. It is structuring, operating and controlling a company with a view to achieving long term strategic goals to satisfy shareholders, creditors, employees, customers and suppliers and to comply with the legal and regulatory requirements, apart from meeting environmental and local community needs.(A. C. Fernando, 1997)

Effective corporate governance reduces “control rights” shareholders and creditors confer on managers, increasing the probability that managers invest in positive net present value projects (Shleifer and Vishny, 1997). Thus, the relationships of the board and the management should be characterized by transparency to shareholders, and fairness to other stakeholders.

2.2 Corporate Governance in Ethiopia

There are a number of companies that are being formed by sale of shares to the wider public unlike most share companies in the past which were formed among founders. (Addis Fortune, (Addis Ababa), April 28, 2011). The emergence of publicly held share companies in Ethiopia gives rise to a multitude of issues on corporate governance. Typically, ownership separates from the control of dispersed shareholders and goes into the hands of few managers, which in turn create the principal-agent relationship in such situations, agents (managers) may misappropriate the principals' (shareholders') investments as they have more information and knowledge than the shareholders. Where there exist few block holders in share companies, minority shareholders could be exploited in the hands of such block holders. The agency problems that could occur between dispersed shareholders and managers and/or block holders of share companies in Ethiopia, therefore, necessitate good corporate governance laws and institutions. (Fekadu (2010)

Minga (2008) observes that the status of corporate governance in Ethiopia is disappointing and notes that “the Commercial Code of 1960 does not provide adequate legislative response to complex governance issues of the day, and the new draft corporate law has not yet been finalized,” and he further states that “key international conventions, codes and standards are not ratified or adequately incorporated in the Proclamations” and that “the Decrees and Directives lack coherence and foresights, and at times suffer from poor drafting.

Fekadu (2010) underlines the growing separation between ownership and control in Ethiopia, and he submits some empirical evidence in this regard. Relying on the data and literature on corporate governance, he shows the deficiency of the Commercial Code in protecting the rights of minority shareholders in the context of publicly held companies. He raises crucial issues such as: “what powers does the board have? Who is it accountable to? How is it organized? What are its standards of liability?” among others.

Tewodros (2011) discusses the legal regime applicable to governance of share companies in Ethiopia. He explores the theoretical background and legal framework of corporate governance and examines the rules of governance in light of available standards. In particular, he discusses the structural choice, appointment and removal, powers, duties and responsibilities, remuneration, and the working methods and mechanism for controlling the boards of directors.

Tewodros states that “a share company is managed by its board which is composed of directors appointed by the general meeting of shareholders.

2.3 Corporate Governance Guidelines for Banking Sector

Given the important financial intermediation role of banks in an economy, their high degree of sensitivity to potential difficulties arising from ineffective corporate governance and the need to safeguard depositors' funds, corporate governance for banking organizations is of great importance to the international financial system and merits targeted supervisory guidance. The Basel Committee on Banking Supervision published guidance in 1999 to assist banking supervisors in promoting the adoption of sound corporate governance practices by banking organizations in their countries. This guidance drew from principles of corporate governance that were published earlier that year by the Organization for Economic Co-operation and Development (OECD) with the purpose of assisting governments in their efforts to evaluate and improve their frameworks for corporate governance and to provide guidance for financial market regulators and participants in financial markets.

The Bank for International Settlements (2006), defined the corporate governance in banks as the methods & approaches used to manage banks through the board of directors and senior management which determine how to put the bank's objectives, operation and protect the interests of shareholders and stakeholders with a commitment to act in accordance with existing laws and regulations and to achieve the protection of the interests of depositors.

Banking companies pose unique corporate governance attention as they differ greatly with other types of firms in terms of broader extent of claimants on the banks assets and funds. A group of entrepreneurs and/or executives could set up a banking business by putting very little equity from their own pocket as the nature of business itself guarantees flow of enormous amount of funds in the form of deposits. The general approach to corporate governance argue in favor of the shareholders rights only, as managers/executives may not always work in the best interest of the shareholders (Jensen, M.C. and Meckling, W.H. (1976), Fama,E. and M. Jensen (1983)

But the shareholders actually account for a very tiny portion of the bank's assets and funds. Rather almost every bit of banks' investments are financed by the depositors' funds. In case of losses or failures it will be depositors' savings that the banks would lose. Such risks demand priority in protection of depositors that ushers in a broader view of corporate governance that suggests the interest and benefits of the suppliers of funds for a firm should be. The self-dealing activities by the bank insiders are very dangerous to the performance and survival of the banks as scores of previous bank failures have been caused by risky self-dealing by the bank insiders (Clarke, 1988).

The presence of heavy liquid assets and potential lack of depositors' interest to actively control and monitor banks' risky decisions as a result of the insurance guarantees simplifies and aggravates the sharking in the banking firms. Banks in developing countries are faced with high risk of sharking as a result of heavy government ownership, lack of prudential regulation, weak legal protection and presence of special interest groups (Arun, T.G. and J. Turner, 2003). However, there is an argument that active role by regulators may cause problems as well, as regulators may not have a convincing or sufficient motivation to monitor the banks as they do not have much at stake in case of bank failures. Recently, the financial markets of developing economies have experienced rapid changes due to the growth of wider range of financial products. As a result of this, banks have been involved with high risk activities such as trading in financial markets and different off balance sheet activities more than ever before (Greuning, H. and S. Bratanovic, 2003), which necessitate an added emphasis on quality of corporate governance of banks in developing economies.

2.4 Corporate Governance Principles review

2.4.1 OECD Principles of Corporate Governance

The following are the OECD Principles of Corporate Governance:

1. The corporate governance framework should promote transparent and efficient markets, be consistent with the rule of law and clearly articulate the division of responsibilities among different supervisory, regulatory and enforcement authorities.
2. The corporate governance framework should protect and facilitate the exercise of shareholders' rights.

3. The corporate governance framework should ensure the equitable treatment of all shareholders, including minority and foreign shareholders. All shareholders should have the opportunity to obtain effective redress for violation of their rights.
4. The corporate governance framework should recognize the rights of stakeholders established by law or through mutual agreements and encourage active co-operation between corporations and stakeholders in creating wealth, jobs, and the sustainability of financially sound enterprises.
5. The corporate governance framework should ensure that timely and accurate disclosure is made on all material matters regarding the corporation, including the financial situation, performance, ownership, and governance of the company.
6. The corporate governance framework should ensure the strategic guidance of the company, the effective monitoring of management by the board, and the board's accountability to the company and the shareholders (OECD, 2004).

2.4.2. Basel Principles of Corporate Governance for banks

- Principle 1: Board members should be qualified for their positions, have a clear understanding of their role in Corporate Governance and be able to exercise sound judgment about the affairs of the bank.
- Principle 2: The board of directors should approve and oversee the bank's strategic objectives and corporate values that are communicated throughout the banking organization.
- Principle 3: The board of directors should set and enforce clear lines of responsibility and accountability through the organization.
- Principle 4: The board should ensure that there is appropriate oversight by senior management consistent with board policy.
- Principle 5: The board and senior management should effectively utilize the work conducted by the internal audit function, external auditors, and internal control functions.
- Principle 6: The board should ensure that compensation policies and practices are consistent with the bank's corporate culture, long-term objectives and strategy, and control environment.
- Principle 7: The bank should be governed in a transparent manner.
- Principle 8: The board and senior management should understand the bank's operational structure, including where the bank operates in jurisdictions, those that may impede transparency (i.e. "know-your-structure"). (The Basel Committee on Banking Supervision, 2005).

2.5 Corporate Governance Theories

For the purpose of this paper various corporate governance theories have been reviewed: agency, stakeholders and resource dependency theory, stewardship theory, social contract theory legitimacy theory and political theory.

2.5.1 Agency Theory

Since the early work of Berle and Means in 1932, corporate governance has focused upon the separation of ownership and pedals which results in principal-agent problems arising from the dispersed ownership in the modern corporation. They regarded corporate governance as a mechanism where a board of directors is a crucial monitoring device to minimize the problems brought about by the principal-agent relationship. In this context, agents are the managers, principals are the owners and the boards of directors act as the monitoring mechanism (Mallin, 2004). Moreover, literature on corporate governance attributes two factors to agency theory. The first factor is that corporations are reduced to two participants, managers and shareholders whose interests are assumed to be both clear and consistent. A second notion is that humans are self-interested and disinclined to sacrifice their personal interests for the interests of the others (Daily, Dalton & Cannella, 2003).

The seminal papers of Alchian and Demsteez (1972) and Jensen and Meckling (1976), describe the firm as a nexus of contracts among individual factors of production resulting in the emergence of the agency theory. The firm is not an individual but a legal fiction, where conflicting objectives of individuals are brought into equilibrium within a framework of contractual relationships. These contractual relationships are not only with employees, but with suppliers, customers and creditors (Jensen & Meckling, 1976). The intention of these contracts is that all the parties acting in their self-interest are motivated to maximize the value of the organization, reducing the agency costs and adopting accounting methods that most efficiently reflect their own performance (Deegan, 2004).

The agency role of the directors refers to the governance function of the board of directors in serving the shareholders by ratifying the decisions made by the managers and monitoring the implementation of those decisions. According to the perspective of agency theory the primary responsibility of the board of directors is towards the shareholders to ensure maximization of shareholder value. The focus of agency theory of the principal and agent relationship (for

example shareholders and corporate managers) has created uncertainty due to various information asymmetries (Deegan, 2004). The separation of ownership from management can lead to managers of firms taking action that may not maximize shareholder wealth, due to their firm specific knowledge and expertise, which would benefit them and not the owners; hence a monitoring mechanism is designed to protect the shareholder interest (Jensen & Meckling, 1976). This emphasizes the role of accounting in reducing the agency cost in an organization, effectively through written contracts tied to the accounting systems as a crucial component of corporate governance structures, because if a manager is rewarded for their performance such as accounting profits, they will attempt to increase profits which will lead to an increase in bonus or remuneration through the selection of a particular accounting method that will increase profits.

Arising from the above is the agency problem on how to induce the agent to act in the best interests of the principal. This results in agency costs, for example monitoring costs and disciplining the agent to prevent abuse (Shleifer & Vishny, 1997). Jensen and Meckling (1976) define agency costs: the sum of monitoring expenditure by the principal to limit the aberrant activities of the agent; bonding expenditure by the agent which will guarantee that certain actions of the agent will not harm the principal or to ensure the principal is compensated if such actions occur and the residual loss which is the dollar equivalent to the reduction of welfare as a result of the divergence between the agents decisions and those decisions that would maximize the welfare of the principal. However, the agency problem depends on the ownership characteristics of each country. In countries where ownership structures are dispersed, if the investors disagree with the management or are disappointed with the performance of the company, they use the exit options, which will be signaled through reduction in share prices. Whereas countries with concentrated ownership structures and large dominant shareholders, tend to control the managers and expropriate minority shareholders in order to gain private control benefits (Spanos, 2005).

The agency model assumes that individuals have access to complete information and investors possess significant knowledge of whether or not governance activities conform to their preferences and the board has knowledge of investors' preferences (Smallman, 2004). Therefore according to the view of the agency theorists, an efficient market is considered a solution to mitigate the agency problem, which includes an efficient market for corporate control, management labor and corporate information (Clarke, 2004).

2.5.2 Stakeholder Theory

This theory centers on the issues concerning the stakeholders in an institution. It stipulates that a corporate entity invariably seeks to provide a balance between the interests of its diverse stakeholders in order to ensure that each interest constituency receives some degree of satisfaction (Abrams, 1951). However, there is an argument that the theory is narrow (Coleman, 2008) because it identifies the shareholders as the only interest group of a corporate entity. However, the stakeholder theory is better in explaining the role of corporate governance than the agency theory by highlighting different constituents of a firm (Coleman, 2008).

With an original view of the firm the shareholder is the only one recognized by business law in most countries because they are the owners of the companies. In view of this, the firm has a fiduciary duty to maximize their returns and put their needs first. In more recent business models, the institution converts the inputs of investors, employees, and suppliers into forms that are saleable to customers, hence returns back to its shareholders. This model addresses the needs of investors, employers, suppliers and customers. Pertaining to the scenario above, stakeholder theory argues that the parties involved should include governmental bodies, political groups, trade associations, trade unions, communities, associated corporations, prospective employees and the general public. In some scenarios competitors and prospective clients can be regarded as stakeholders to help improve business efficiency in the market place.

Stakeholder theory has become more prominent because many researchers have recognized that the activities of a corporate entity impact on the external environment requiring accountability of the organization to a wider audience than simply its shareholders. For instance, McDonald and Puxty (1979) proposed that companies are no longer the instrument of shareholders alone but exist within society and, therefore, has responsibilities to that society. One must however point out that large recognition of this fact has rather been a recent phenomenon. Indeed, it has been realized that economic value is created by people who voluntarily come together and cooperate to improve everyone's position (Freeman et. al., 2004). Jensen (2001) critiques the Stakeholder theory for assuming a single-valued objective (gains that accrue to a firm's constituency). The argument of Jensen (2001) suggests that the performance of a firm is not and should not be measured only by gains to its stakeholders. Other key issues such as flow of information from senior management to lower ranks, interpersonal relations, working environment, etc. are all critical issues that should be considered. Some of these other issues provided a platform for other

arguments. An extension of the theory called an enlightened stakeholder theory was proposed. However, problems relating to empirical testing of the extension have limited its relevance (Sanda et. al., 2005).

In order to differentiate among stakeholder types, Rodriguez et al., (2002): classification was adopted; consubstantial, contractual and contextual stakeholders. Consubstantial stakeholders are the stakeholders that are essential for the business's existence (shareholders and investors, strategic partners, employees). Contractual stakeholders, as their name indicates, have some kind of a formal contract with the business (financial institutions, suppliers and sub-contractors, customers). Contextual stakeholders are representatives of the social and natural systems in which the business operates and play a fundamental role in obtaining business credibility and, ultimately, the acceptance of their activities (public administration, local communities, countries and societies, knowledge and opinion makers). Rajan and Zingales (1998) argue that the company has to safeguard the interests of all who contribute to the general value creation, that is, make specific investments to a given corporation. These firms-specific investments can be diverse and include physical, human and social capital.

2.5.3 Resource Dependency Theory

The basic proposition of resource dependence theory is the need for environmental linkages between the firm and outside resources. In this perspective, directors serve to connect the firm with external factors by co-opting the resources needed to survive (Pfeffer and Salancik, 1978). Thus, boards of directors are an important mechanism for absorbing critical elements of environmental uncertainty into the firm. Williamson (1985) held that environmental linkages or network governance could reduce transaction costs associated with environmental interdependency. The organization's need to require resources and these leads to the development of exchange relationships or network governance between organizations. Further, the uneven distribution of needed resources results in interdependence in organizational relationships. Several factors would appear to intensify the character of this dependence, e.g. The importance of the resource, the relative shortage of the resource and the extent to which the resource is concentrated in the environment (Donaldson and Davis, 1991).

Additionally, directors may serve to link the external resources with the firm to overwhelm uncertainty (Hillman, Cannella Jr & Paetzols, 2000), because managing effectively with uncertainty is crucial for the existence of the company. According to the resource dependency rule, the directors bring resources such as information, skills, key constituents (suppliers, buyers, public policy decision makers, social groups) and legitimacy that will reduce uncertainty (Gales & Kesner, 1994). Thus, Hillman et al. (2000) consider the potential results of connecting the firm with external environmental factors and reducing uncertainty is decrease the transaction cost associated with external association. This theory supports the appointment of directors to multiple boards because of their opportunities to gather information and network in various ways.

2.5.4 Stewardship Theory

In contrast to agency theory, stewardship theory presents a different model of management, where managers are considered good stewards who will act in the best interest of the owners (Donaldson & Davis 1991). The fundamentals of stewardship theory are based on social psychology, which focuses on the behavior of executives. The steward's behavior is pro-organizational and collectivists and has higher utility than individualistic self-serving behavior and the steward's behavior will not depart from the interest of the organization because the steward seeks to attain the objectives of the organization (Davis, Schoorman & Donaldson 1997). According to Smallman (2004) where shareholder wealth is maximized, the steward's utilities are maximized too, because organizational success will serve most requirements and the stewards will have a clear mission. He also states that, stewards balance tensions between different beneficiaries and other interest groups. Therefore stewardship theory is an argument put forward in firm performance that satisfies the requirements of the interested parties resulting in dynamic performance equilibrium for balanced governance.

Stewardship theory sees a strong relationship between managers and the success of the firm, and therefore the stewards protect and maximize shareholder wealth through firm performance.

A steward who improves performance successfully satisfies most stakeholder groups in an organization, when these groups have interests that are well served by increasing organizational wealth (Davis, Schoorman & Donaldson 1997). When the position of the CEO and Chairman is held by a single person, the fate of the organization and the power to determine strategy is the

responsibility of a single person. Thus the focus of stewardship theory is on structures that facilitate and empower rather than monitor and control (Davis, Schoorman & Donaldson 1997). Therefore stewardship theory takes a more relaxed view of the separation of the role of chairman and CEO, and supports appointment of a single person for the position of chairman and CEO and a majority of specialist executive directors rather than non-executive directors (Clarke 2004).

2.5.5 Social Contract Theory

Among other theories reviewed in corporate governance literature social contract theory, sees society as a series of social contracts between members of society and society itself (Gray, Owen & Adams 1996). There is a school of thought which sees social responsibility as a contractual obligation the firm owes to society (Donaldson 1983). An integrated social contract theory was developed by Donaldson and Dunfee (1999) as a way for managers make ethical decision making which refers to macro social and micro social contracts. The former refers to the communities and the expectation from the business to provide support to the local community, and the latter refers to a specific form of involvement.

2.5.6 Legitimacy Theory

Another theory reviewed in the corporate governance literature is legitimacy theory. Legitimacy theory is defined as “a generalized perception or assumption that the actions of an entity are desirable, proper, or appropriate with some socially constructed systems of norms, values, beliefs and definitions” (Suchman 1995). Similar to social contract theory, legitimacy theory is based upon the notion that there is a social contract between the society and an organization. A firm receives permission to operate from the society and is ultimately accountable to the society for how it operates and what it does, because society provides corporations the authority to own and use natural resources and to hire employees (Deegan 2004).

Traditionally profit maximization was viewed as a measure of corporate performance. But according to the legitimacy theory, profit is viewed as an all inclusive measure of organizational legitimacy (Ramanathan 1976). The emphasis of legitimacy theory is that an organization must consider the rights of the public at large not merely the rights of the investors. Failure to comply with societal expectations may result in sanctions being imposed in the form of restrictions on the firm's operations, resources and demand for its products (Deegan, 2004).

2.5.7 Political Theory

Political theory brings the approach of developing voting support from shareholders, rather by purchasing voting power. Hence having a political influence in corporate governance may direct corporate governance within the organization. Public interest is much reserved as the government participates in corporate decision making, taking into consideration cultural challenges (Pound, 1983). The political model highlights the allocation of corporate power, profits and privileges are determined via the governments' favor. The political model of corporate governance can have an immense influence on governance developments. Over the last decades, the government of a country has been seen to have a strong political influence on firms. As a result, there is an entrance of politics into the governance structure or firms' mechanism (Hawley and Williams, 1996).

CHAPTER THREE

METHODOLOGY

This chapter presents methods used in carrying out the study. In particular, this study was employed in order to describe the extent to which corporate governance practices are applied in the Ethiopian private commercial banks, the case of DB. It presents the research design, procedures of data collection, the instruments used to gather the necessary data, the sampling procedure and finally method of data analysis and presentation.

3.1 Research Design

The type of research employed for the purpose of this study is descriptive in nature, because, the researcher has no control or effect on the variables of the study. It was intended only to investigate the extent to which corporate governance principles are implemented in the Ethiopian private commercial banks, the case of Dashen Bank.

Descriptive study is helpful when a researcher wants to look into a phenomenon or a process in its natural contexts in order to get its overall picture instead of taking one or some of its aspects and manipulating it in a simulated or an artificial setting. (Seiliger and Shohamy 1989; McDonough 1997).

Thus, descriptive study was chosen to assess the extent to which corporate governance principles are implemented in banks from a holistic perspective in its natural settings. Moreover, in order to achieve the intended objective both quantitative and qualitative methods were chosen. Hence, the convenient research design considered suitable for this study was descriptive case study.

3.2. Data Sources and Methods of Data Collection

To make the research output thorough, a triangulated list of methods of data collection instruments were employed. The data were collected both from the primary data sources (using questionnaire and interview) and the secondary data sources. As Moser and Kalton (1972) suggests, the use of different instruments for a study provides a powerful research strategy. As part of the primary data, a comprehensive questionnaire (a copy was placed as appendix A at the end of the report) was designed and distributed to all board members of the target bank. In

addition, interview with four board members, the senior manager and the board secretary was conducted to obtain detailed information.

Primary data have been collected through questioners which was designed and distributed to board members of the target bank and senior managements. In addition, interview with two board members and five senior managers was conducted to obtain detailed information. Secondary data have been collected from different journals, books banks website and banks annual reports.

The questionnaire consists of close ended questions. The questionnaire has been developed based on the corporate governance codes for Basel, OECD and NBE.

Interview was prepared to substantiate the results obtained from the questionnaire thereby to get a greater depth of information. This means of data collection instrument helps the researcher to get reliable information from the target population that how they feel and think about the problem. Interview according to Arikunto (2002) is a kind of dialogue which is done by an interviewer to get reliable information from an interviewee.

Consequently, the purpose of the interview was to substantiate the results obtained from the questionnaire thereby to get a greater depth of information. The interview questions were prepared in a semi structured type. There were a total of 5 questions asked to two board members and five senior managers.

3.3 Target Population and Sampling Methods

The target populations of this study are the senior managers and board members of Dashen Bank. Based on the information found from the National Bank of Ethiopia, there were a total of 9 board members for the Dashen bank. All of them were taken as a target population for the purpose of this study. And the other target population of the study was the bank's senior manager in other ways; a population census was used to make the research. In a nutshell, a total of 30 participants, 4 board members and 26 senior managers with minimum of ten years experience were involved in the study.

Finally, the kind of sampling techniques used for the selection of the participants so as to conduct this research was non probability sampling technique under which purposive sampling technique has been used to gather primary data.

3.4. Measuring methods

Scales Include 5 point Liker scales. Where 1= strongly disagree, 2=disagree, 3=undecided 4= agree, 5= strongly agree

3.5. Data Analysis Method

In this step, each element of the major issues of corporate governance has been tabulated and analyzed. Particularly for the quantitative data collected via the questionnaire, a descriptive Statistical analysis method and excel spread shit was used to tabulate the data and present it in tables.

Since the data obtained through interview was used to back the information gained through questionnaires qualitative method of data analysis was employed.

3.6 Ethical Consideration

Before the research was conducted on the selected bank, the researcher informed the participants of the study about the objectives of the study, and was consciously consider ethical issues in seeking consent, avoiding deception, maintaining confidentiality, respecting the privacy, and protecting the anonymity of all respondents. A researcher must consider these points because the law of ethics on research condemns conducting a research without the consensus of the respondents for the above listed reasons.

CHAPTER FOUR

RESULT AND DISCUSSION

In this section, the collected data were discussed, analyzed and presented. In doing so, the data gathered through the questionnaire were presented in tables. Apart from this, the data collected through interview were merged together and interpreted with the result of the questionnaire. This chapter generally consists of presentation of the statistical results obtained, illustrated tables, discussions of the results obtained from the questionnaire and interview of the target population.

4.1. Description of Dashen Bank

Dashen Bank which is established in 1995 coined its name from the highest peak in the Country mount Dashen and aspires to be unparalleled in banking. Headquartered in Addis Ababa, the Bank is the biggest private Bank in Ethiopia. It operates through a network of 150 Area Banks, five dedicated Forex Bureaus, 170 ATMs and 827 plus Point-of-Sale (POS) terminals spread across the length and breadth of the nation. It has established correspondent banking relationship with 454 banks covering 70 countries and 166 cities across the world. Wherever business takes customers around the world Dashen Bank is already there. Dashen is the most reputable brand in the domestic banking market a reputation earned through consistent delivery of values and preeminence unmatched by its competitors. The Bank also works in partnership with leading brands in the electronic payments industry (VISA, MasterCard, America Express & Union Pay) and prominent money transfer operators (Western Union, MoneyGram, Express Money, Dahabshiil, & Trans Fast).

Current Status

The Bank, which was established with a paid up capital of Birr 14.9 million, has grown in leaps and bounds in the past 19 years. The following figures indicate the position of the Bank as at June 30, 2014, the closing date of the last fiscal year. Total assets ETB 22 billion, Deposits ETB 17.7 billion, Loans & advances ETB 9.4 billion and Profit before tax ETB 957.6 million.

Products and services

Deposit Accounts

- **Savings Account**
- **Current Account**
- **Fixed Time Deposit**
- **Hybrid Account**
- **Saving plus Account**
- **Student Account**
- **Modified Youth Savings Account**
- **Interest plus Bonus Account**
- **Current Account Protection Scheme**
- **Loans and Advances**
- **Foreign Currency Depository Account**

Payment Card Services

Dashen Bank is the first bank in Ethiopia to provide a full-fledged payment card service as a principal plus member of VISA, MasterCard and UnionPay (as the first African Bank to sign such agreement). The Bank issues VISA branded Dashen debit card that give clients the added convenience of round-the-clock banking through Automated Teller Machines (ATMs) and conduct POS purchase at a growing number of merchant locations. Customers have access to 170 ATMs and 827 plus POS terminals spread across strategic and convenient places. The Bank also starts accepting American Express (AmEX) card on its ATMs and POS terminals. Currently, more than a quarter of a million customers use Dashen Debit Card. Dashen Bank has established ATM interoperability with Zemen Bank under the umbrella of its principal VISA membership right to extend the technology to other Banks and enable them to be associate VISA members.

Governance structure

The bank governance structure is made up of nine board members under whom 18 policy development committee members and other specialty committees are included. The board is lead by a non executive board chair man who is directly responsible to the shareholders of the bank.

4.2 Respondents profile

Table 4.1. Respondents profile by sex and Age group

GENDER		frequency	%							
	M	30	100							
	F									
	Under 30		30 to 45		45 to 60		60 or older		Total	
Age(SM)	F	%	F	%	F	%	F	%	F	%
			18	69.2	8	30.8			26	100
	Under 30		30 to 45		45 to 60		60 or older		Total	
Age(BOD)	F	%	F	%	F	%	F	%	F	%
			2	50	2	50	0	0	4	100

Source: Survey data

The above figure shows sex and age distribution of the respondents. The table is divided in to three parts which are the sex, profile, age of senior managers as well as the board. In the first part the survey shows that all the respondents are male. For the second part of the table which is age of senior managers most frequent age interval is 30-45 years which is 69.2% of the senior manager's sample the other 30.8% of the respondents are in the age group of 45-60. In the second group from the total sample taken from the board 50% of the respondents were between 30 and 45 and the other 50% are between the ages of 46 to 60. The result is consistent with the new directive Banking Business Proclamation 592/2008 issued by the National Bank of Ethiopia that a member of the board of a bank has to be at least 30 years old.

Table 4.2. Educational Background

Category of respondents	Diploma		Degree		Masters		PhD		others	
BOD	F	%	F	%	F	%	F	%	F	%
			1	25	3	75				
SM			16	61.5	10	38.5				
TOTAL			17	56.6	13	43.4				

Source: Survey data

Among the sample respondents of the board 25% of the samples are Degree holder and 75% of the sample is a master degree holder which meets the National Bank's 2008 directive, which requires that at least 75% of a bank's board members hold a minimum of a first degree or equivalent from a recognized higher learning institution. The educational levels of senior manager respondents show that 61.5% of them have degree and the other 43.4% of the respondents have master degree.

The result also indicated that the above requirement set by the National Bank has resulted in the selection of directors with good academic preparation and experience Moreover, the professional level of the directors as well as senior managers can improved understanding between management and members of the Board.

Table.4.3. Respondents profile by Work experience

Year	Frequency	Percentage
9-20	26	86.7
21-30	3	10
31 and above	1	3.3
Total	30	100

Source: Survey data

Basel,(2014) stated that directors should have relevant experience which enables the directors to have a clear understanding of their role in corporate governance, which is one of the critical elements of corporate governance.

The above table indicates the work experience of the board respondents which is 3 (10% of the total sample) is between 21-30 years of relevant experience the other 1 (3.3% of the total sample) is between 31 and above which satisfies National Bank of Ethiopia directive that members of a board should have adequate managerial experience, preferably in banking and/or should undergo adequate training in banking business management when holding a seat on the board.

The other 26 (86.7%) of the respondents have 9-20 years of experience in the Bank which all are senior managers of the bank. This implies that, the bank is equipped with well experienced staffs.

4.3. Corporate Governance Practices

In companies with dispersed ownership, shareholders are usually unable to closely monitor management, its strategies and its performance for lack of information and resources(Fekadu 2010) Thus, the role of the board of directors is to fill this gap between the uninformed shareholders as principals and the fully informed executive managers as agents by monitoring the agents more closely(*Ibid*).

Table 4.4 the roles and responsibilities of BOD

No		1		2		3		4		5	
		F	%	F	%	F	%	F	%	F	%
1	Approves the banks strategic plan.									30	100
2	Monitors the implementation of the strategic plan					7	23.3	10	33.3	13	43.4
3	Oversees implementation of the appropriate governance framework.			2	6.7	3	10			25	83.3

4	Adheres to corporate culture.					2	6.7	6	20	22	73.3
5	BOD monitors the senior management action.							9	30	21	70
6	The board ensures that appropriate succession is in place for senior management position.	6	20	20	66.7	4	13.3				
7	Continuously ensures the skill of internal audit.					3	10	23	76.7	4	13.3

Source: Survey data

The above table shows different criteria that can be used to evaluate the roles and responsibilities of the board and the respondents were asked whether or not they are practically used in the bank. Accordingly, the frequency distribution and percentage value of the usage of the above criteria is presented as follows.

The first criterion as shown in the above table is ‘approval of the banks strategic plan’ in this respect, the survey indicates that 100% of the respondents are strongly agreed, which shows this criterion is practically applied in the bank.

According to NBE directive 2014 under sub-article 6.6.2. the board is responsible for reviewing and approving strategies, policies, procedures/guidelines, annual business plans & budgets. Which is also stated in basel (2014), the board has overall responsibility for the bank including approving and overseeing the implementation of the bank’s strategic objectives.

As per ioD (2010) the board should delegate authority to management and to monitor and evaluate its implementation of policies, strategies, and operational plans.

According to the above table, 43.4% of the sample strongly agreed that the board monitors the implementation of the strategic plan the other 33.3% of the sample also agreed the board is somehow monitors the implementation of the approved plans the other 23.3% of the sample stay neutral. This criterion is therefore revealed by majority of the respondents as it has been carried out by the board, they show their agreement. Which is also goes along with NBEs directive article 6.6.3 (2014) the board also have to monitoring management’s performance in implementing the approved strategic plans of the bank.

The third criterion indicated in the above table is “Oversees implementation of the appropriate governance framework” responded by 6.7%, 10%, and 83.3% of the respondents that they were disagree, undecided and strongly agreed. Therefore, as the result shows more than half of the respondents show their agreement as the board oversees implementation of the appropriate governance framework. According to Basel Committee for Banking Supervision (2014), the board should review the governance framework periodically and monitors its implementation so that it remains appropriate in the light of material changes in the bank’s size, complexity, geographic reach, business strategy, market, governance best practices, and regulatory requirements.

Basel Committee for Banking Supervision (2014) stated that the board should adhere to corporate values for itself and make sure that senior management and other employees that create expectations that all business should be conducted in a legal and ethical manner.

The fourth criterion as shown in the above table is ‘weather the board adheres to corporate culture or not’ in this respect, the survey indicates that 73.3% of the respondents are strongly agreed that the board adheres to the banks corporate culture and goes with the principles also 20% of the respondents support the above answer by agreeing with the above concept but the other 6.7% of the respondents were not in the position to decide about the question.

According to the table the respondents response on whether the board monitors senior management’s action or not were 30% and 70% agreed and strongly agree respectively.

Sebi, (2000) stated that the board of directors of a company should direct and controls the actions of the management. Accordingly the above result shows that the board of the bank monitors the senior managers’ action which also supported by the interview responses in which the board monitors the managers’ action through different mechanisms like internal control, online reporting system on daily basis like outlook and link communication systems and evaluates their performance periodically. Also in relation with that the board monitors senior managers from using the resources of the bank to their own use by manipulating their power to their own sake via limiting their discretionary power on banks recourses and setting up effective check and balance system through internal control. Fama and Jensen (1983) also support this by characterizing the responsibilities of the board of directors as being both the ratification of management decisions and the monitoring of management performance.

The final draft of NBE directive (2014) on corporate governance of banks states that the board should approve succession plan policy for chief executive officer and senior executive officers and effectively monitor its implementation.

According to the table the response of the respondents on the succession plan of the bank is 20%, 66.7% and 13.3% strongly disagreed, disagreed and undecided respectively which can be interpreted as the bank do not have any written succession plan for senior managers which also was one of the major duties of the board. As per Basel Committee for Banking Supervision (2014) the board should ensure that appropriate succession plans are in place for senior management positions.

The most effective method of preventing and detecting fraud is an adequate system of internal controls. Internal controls are put in an accounting system to safeguard the assets of the organization, check the accuracy and reliability of its accounting data, promote operating efficiency and encourage adherence to prescribed managerial policies. An adequate system of internal controls tends to prevent defalcation by reducing the opportunity and therefore the temptation to misuse the bank's assets (Basel Committee for Banking Supervision, 2014). The committee also stated that the board should ensure that the internal audit functions are properly positioned staffed and resourced and carries out their responsibilities independently and effectively.

Accordingly criterion number 8 'The board continuously ensures the skill of internal audit.' is replied by most of the respondents (76.7%) that they agreed on continues skill assessment of internal auditors by the board of the bank 13.3% of the respondents also strongly agreed with the application of the above concept in the bank but the other 10% of the respondents stayed undecided. From which it can be concluded that as internal control is the base for well functioning of the bank as well as efficient resource utilization and success of the company the board of the bank are carrying out their responsibility on continuous assessment of the banks internal auditors.

Table 4.5 **Qualification and composition of BOD**

No	Items	1		2		3		4		5	
		F	%	F	%	F	%	F	%	F	%
1	Sufficient knowledge in relevant areas.					9	30	15	50	6	20
2	Sufficient experience in relevant areas.					3	10	24	80	3	10
3	Sufficient time to fully carryout their responsibilities.	4	13.3	9	30	6	20	8	26.7	3	10
4	Do not have personal relationship with other members of the board.	5	16.6	12	40	8	26.7	5	16.6		
5	Do not have economic relationship with other members of the board.	2	6.7	17	56.7	7	23.3	4	13.3		
6	The shareholders ensure board members have access to ongoing training on relevant issues.					7	23.3	16	53.4	7	23.3
7	Comprises the minimum number of required independent number of board members.					4	13.3	9	30	17	56.7

Source: Survey data

The Basel committee for Banking Supervision (2006) recommends Board members should be and remain qualified individually and collectively for their positions. They should understand their oversight and corporate governance role and be able to exercise sound, objective judgment about the affairs of the bank. It also mentioned that having sufficient knowledge about board functions and the company is a very important element of the good corporate governance. Being knowledge full is an indicator that the board members can undertake their functions properly.

Accordingly on the issue of the knowledge of the board members the table illustrates 50% of the respondents agreed that the board has Sufficient knowledge in relevant areas to lead the bank smoothly in relation with that 20% of the sample also strongly agreed on the issue and believes

that the board members has sufficient knowledge in relevant areas which helps them to oversee the bank soundly.

As it is said experience makes as perfect the above table demonstrates 10%, 80% and 10% for undecided, agreed and strongly agreed which can be interpreted as the board members has sufficient work experience on relevant areas for the business which is supported by 80% which is agreed and 10% strongly agreed in which the experience of the board members is in accordance with the NBE (2014) directive which mentions at least two of the board members of a bank shall be qualified or experienced in finance related disciplines.

As per CCANB (1998) to effectively supervise the bank's affairs and become informed about the bank's affairs the BOD members should have sufficient time for their duties.

But as it is shown in the above table the majority of the respondents which are 30% and 13.3% disagreed and strongly disagreed respectively that the board members do not have sufficient time to effectively monitor the bank as the other 20 % stayed neutral where as 26.7% and 10% of the respondents believes that the present time is sufficient for the board to Carry out their duty effectively by scoring agreed and strongly agreed respectively.

In the same fashion, the result of the researcher observation also displays that the board members are very busy for many of the board members of the bank also work in other organizations in addition to their full time business. This reality has also been obvious during the research work that most of the board members have taken too much time to fill the questionnaire while it is a matter of hours work. The OECD principles of corporate governance also states that the board should have sufficient time to fully carry out their responsibilities.

The corporate governance principles strongly require that a board member should be independent and be free from any personal relationships. But the majority of the sample which is 16.6% and 40% of the respondents strongly disagreed and disagreed respectively to explain their view that some of the board members have personal relationship which is against the corporate governance principles but the other 16.6% believes that the board members are free from personal relationship with each other while the other 26.7% are unable to decide.

Basel (2014) also mentioned that members of the board should not have any personal, professional or other economic relationships with other members of the board or management (or

with other entities within the group) but the survey reflects against the principle which is some of the members have economic dependency with each other which is shown on the above table that 6.7% and 56.7% of the total sample strongly disagreed and disagreed on the issue the other 23.3% and 13.3% are undecided and agreed respectively.

The Bank shall give training to directors at least once in a year as sited in CG principles on areas of financial analysis, corporate governance, applicable laws, regulations and directives and risk management and internal control.

For criterion number 6 the above table 53.4% of the respondents scored agreed and illustrated that the banks shareholders make sure that the board members participated in different training issues which are relevant to the bank as well as to ensure and develop their skill and knowledge of governance which is also shared by 23.3% of the respondents who strongly agreed with the issue while the other 23.3% of the sample are impartial.

The bank should have sufficient number of independent board members, who are responsible for different roles in the board to undertake independently. In this regard the above table shows 56.7% of the respondents scored strongly agreed and illustrated that the board comprises sufficient number of independent members. As shown in the table 30% of the respondents also agreed that the board has the required number of independent members while the other 13.3% are neutral on the point. The corporate governance principles strongly require that a board should comprise independent member that should exercise an independent judgment and be free from any influence to the contrary. “All processes, decision making and mechanisms used should be established so as to minimize or avoid potential conflicts of interest.”

Table 4.6 Structure and practices

No	Items	1		2		3		4		5	
		F	%	F	%	F	%	F	%	F	%
1	The board periodically reviews its structure.							11	36.7	19	63.3
2	The chair of the board is non executive board member.							16	53.3	14	46.7
3	There is a mechanism that minority	9	30	13	43.3	8	26.7				

	shareholders vote to the BOD.										
4	There is a formal procedure for selecting board members.					6	20	14	46.7	10	33.3

Source: Survey data

To support its own performance, the board should carry out regular assessments alone or with the assistance of external experts of the board as a whole, its committees and individual board members. The board should periodically review its structure (basel, 2014).

As stated in the above table 36.7% and 63.3% of the sample agreed and strongly agreed respectively by which the board reviews its structure periodically.

According to the OECD Principles of Corporate Governance, “In order to improve board practices and the performance of its members the board should review itself periodically.

The table shows that 53.3% and 46.7% of respondents responded agreed and strongly agreed that the chair of the board is non-executive board member. As per Basel committee for Banking Supervision (2014) to promote checks and balances the chair of the board should be a non-executive board member.

The Board Standing Nomination Committee shall give equal opportunity to all shareholders in nominating potential candidate for a seat on the board (NBE, 2014). But as illustrated above on the table the majority of the respondents which are 30% (strongly disagreed) and 43.3% (disagreed) demonstrates that there is no mechanism for minority shareholders to give their vote equally with the other shareholders the other 26.7% of the respondents were not ready to decide

For criterion number 4, 20% of the respondents were neutral while the majority of the sample which are 46.7% and 33.3% were scored agreed and strongly agreed by which the bank has formal procedures for selecting board members. As per the national bank directives (2014) the Boards should have a clear and rigorous process for identifying, assessing and selecting board candidates. Unless required otherwise by law, the board (not management) identifies and nominates candidates and ensures appropriate succession planning of board members and senior management.

Table 4.7 **Risk management**

No	Items	1		2		3		4		5	
		F	%	F	%	F	%	F	%	F	%
1	The risk management of the bank is independent.	7	23.3	16	53.3	3	10	4	13.4		
2	The bank has an approved risk limit.							3	10	27	90
3	The risk management continuously identifies the risk exposures of the bank.									30	100

Source: Survey data

For the first criteria 23.3% and 53.3% of the respondents believes that the risk management committee of the bank is not free from influence on making decisions but the other 13.4% of the respondents agreed that the committee is independent and can make the required decisions without influence the other 10% of the sample stayed neutral. But as per basel (2014) banks and banking groups must have independent risk management processes (including Board and senior management oversight) to identify, evaluate, monitor and control or mitigate all material risks and to assess their overall capital adequacy in relation to their risk profile.

Boards of directors have ultimate responsibility for the level of risk taken by their institutions. Accordingly, they should approve the overall business strategies and significant policies of their institutions, including those related to managing and taking risks. (SFI, 2007)

Accordingly as per the above table 10% and 90% of the respondents agreed and strongly agreed on the point that the bank has approved risk limit.

National bank directives on corporate governance of banks also states that the board ensures that the bank puts in place comprehensive risk management program.

As per SFI, (2007) in order to properly manage risks an institution must recognize and understand risks that may arise from both existing and new business initiatives. For example, risks inherent in lending activity include credit, liquidity, interest rate and operational risks. Risk

identification should be a continuing process and should be understood at both the transaction and portfolio levels.

The above table shows that 100% of the respondents agreed that the banks risk management committee continuously identifies the risk exposures of the bank in order to safe guard the banks benefit and interest.

Table 4.8 Audit

No	Items	1		2		3		4		5	
		F	%	F	%	F	%	F	%	F	%
1	The bank establishes an independent internal audit system.					4	13.3	16	53.3	10	33.4
2	The internal audit has direct access to the BOD.							8	26.7	22	73.3
3	The report of internal auditors does not filtered by senior managers.							17	56.7	13	43.3
4	The audit committee is made up of non-executive directors.							3	10	27	90

Source: Survey data

The internal audit function provides independent assurance to the board and supports board and senior management in promoting an effective governance process and the long-term soundness of the bank. The internal audit function should have a clear mandate, be accountable to the board, be independent of the audited activities and have sufficient standing, skills, resources and authority within the bank. (basel 2014)

As shown in table 5, 53.3% and 33.4% of the respondents agreed and strongly agreed on the point that the bank established an independent audit system. While the other 13.3% are unable to decide from this it can be concluded that the bank has an independent audit system.

According to the corporate governance principles the internal auditors should have a way to communicate directly with the board in relevant matters as per the above table 26.7% and 73.3%

of the sample agreed and strongly agreed on the criteria that the bank has a direct communication system for the internal auditors to communicate with the board.

Base (2014) also suggested that the board and senior management should respect and promote the independence of the internal audit function by ensuring that internal audit reports are provided to the board without management filtering and that the internal auditors have direct access to the board or the board's audit committee. Accordingly the above survey demonstrates that 56.7% and 43.3% of the respondents agreed and strongly agreed respectively on the point that the senior management of the bank did not filter the report of the internal auditors.

According to ACCA (2012) this committee should be made up of independent non-executive directors with at least one individual having expertise in financial management. It is responsible for:

- Oversight of internal controls; approval of financial statements and other significant documents prior to agreement by the full board
- Liaison with external auditors
- High level compliance matters
- reporting to the shareholders.

In relation with the above concept the survey shows that 10% and 90% of the total respondents are positive that the audit committee is made up of non executive directors which are the ground base for the independency of the committee.

Table 4.9 Disclosure

No	Item	1		2		3		4		5	
		F	%	F	%	F	%	F	%	F	%
1	The bank discloses appropriate matters to shareholders							2	6.7	28	93.3
2	The bank discloses appropriate matters to other stakeholders.							25	83.3	5	16.7

3	The bank periodically discloses its corporate governance code to shareholders.					3	10	15	50	12	40
4	All disclosures with shareholders made available on internet in a timely fashion.	8	26.7	18	60	4	13.3				

Source: Survey data

According to OECD principles the corporate governance framework should ensure that timely and accurate disclosure is made on all material matters regarding the corporation. For criteria number 1 of the above table almost all 93.3% of the total sample strongly agreed that the bank discloses appropriate matters to its share holders and also the other 6.7% of the sample supports the above idea by agreeing with the sited point.

Basel principles of corporate governance for banking states that disclosure should be accurate, clear and presented such that shareholders, depositors, other relevant stakeholders and market participants can consult the information easily. Timely public disclosure is desirable on a bank's public website, in its annual and periodic financial reports, or by other appropriate means. It is good practice to have an annual corporate governance-specific and comprehensive statement in a clearly identifiable section of the annual report depending on the applicable financial reporting framework. All material developments that arise between regular reports should be disclosed to the bank supervisor and relevant stakeholders as required by law without undue delay. Accordingly the survey shows that the bank discloses appropriate matters to other stakeholders of the bank which is supported by 83.3% and 16.7% of the respondents by agreeing and strongly agreeing respectively to express their firm believe that the bank disclosure is also made to other stakeholders on relevant areas.

On the third criteria 50% and 40% of the total sample also agreed and strongly agreed that the corporate governance code of the bank is periodically disclosed to all shareholders of the bank while the other 10% of the respondents stayed neutral. Which is sited in basel (2014) principles of corporate governance for banks as The governance code of the bank should be adequately transparent to its shareholders.

For the last criteria of table six majority of the respondents 26.7% and 60% were under strongly disagreed and disagreed category respectively that the bank did not make available all disclosures on the official website of the bank or other internet online means's while the other 13.3% are impartial to give comment. This idea was also backed by the interview which shows the bank online and public disclosers are filtered and shows more of the banks positive side which is against the corporate governance rules which states that the bank should also disclose key points concerning its risk exposures and risk management strategies without breaching necessary confidentiality. When involved in complex or non-transparent activities, the bank should disclose adequate information on their purpose, strategies, structures, and related risks and controls.

Table 4.10 **Compensation**

No	Items	1		2		3		4		5	
		F	%	F	%	F	%	F	%	F	%
1	The banks compensation structure is aligned with sound risk management.					3	10	19	63.3	8	26.7
2	The compensation structure promotes long term health of the organization.					8	26.7	16	53.3	6	20
3	The banks remuneration committee is independent.							1	3.3	29	96.7

Source: Survey data

According to basel (2014) the bank's compensation structure should be effectively aligned with sound risk management and should promote long term health of the organization and appropriate risk-taking behavior.

The above survey shows that 10%, 63.3% and 26.7% of the total sample scores undecided, agree and strongly agree which means that the banks compensation structure is aligned with sound risk management system and also promotes long term health of the organization as per the result of criteria number 2 which shows 26.7%, 53.3% and 20% of the respondents choose undecided, agree and strongly agree respectively with the point sited which is also in line with the corporate governance principle of banks which is also reflected in the interview that the bank ensures long

term interest of its employees through providing deferent benefit schemes and attractive remuneration and compensation structures which also is aligned with its long term interest and significantly decreases the banks employee turnover and creates sound organizational structure and position.

The principles also mentioned that the remuneration committee should be constituted in a way that enables it to exercise competent and independent judgment on compensation policies and practices and the incentives created for managing risk, capital and liquidity.

In the same manner the bank establishes an independent remuneration committee as 96.7% and 3.3% of the total sample strongly agree and agree respectively on the criteria of remuneration committee independence.

Finally the last but not the least the interview respondents were asked to give their comment about the existing corporate culture of the bank their response is summarized under.

Some of the respondent's believes that the bank has good governance culture and should maintain it for its long term success while other suggested that the banks corporate culture is under progress and there should be a lot of things to be included and adjusted to go along with the international as well as national corporate governance principles and laws respectively.

CHAPTER FIVE

SUMMARY AND RECOMMENDATIONS

This chapter provides the reader the summaries of the research analysis, conclusion which discuss the major finding, contribution of this thesis to literature & for policy making and end up with recommendations.

5.1 Summary

The following findings were drawn according to the discussion and analysis of the data presented in the above chapter,

The board of the bank undertakes its roles and responsibilities of approves the banks strategic plan, monitors the implementation of the bank strategic plan, oversees implementation of the appropriate governance framework, adheres to the bank corporate culture, monitors the senior management action closely enough and continuously ensures the skill of internal audit to create sound internal control system in the bank..

But the board did not to create a succession plan in place for senior management position which was one of the board responsibilities.

Concerning the qualification and compositions of the board, the study revealed that board comprises the minimum number of required independent members who have sufficient knowledge and experience in relevant areas which are important for the bank governance. The shareholder of the bank also ensures that the board members of the bank have access to ongoing training on relevant areas to insure the skills of the members.

But the study also revealed that the members do not have sufficient time to carry out their responsibilities as they have deferent part time jobs apart from this and also some of the board members have personal as well as economic relationship with each other.

The board structure is periodically reviewed according to the study. Accordingly the board has a practice of formally selecting board members one of which is non executive board chair. But beside all the good practices the bank fails to have mechanism to minority shareholders to vote to the BOD.

Concerning the risk management of the bank the survey concludes that the bank has an approved risk limit accordingly the risk management continuously identifies the risk exposures of the bank and takes measures according with the risk limits of the bank.

According to the survey the bank risk management system is not fully independent on carrying out its responsibilities.

For the audit system of the bank has an independent internal audit system and lead by the audit committee which is made up of non executive directors. The internal auditors directly communicate with the board and reports to the board without any filtration by senior managers.

Concerning the bank disclosures the survey concludes that the bank discloses appropriate matters to its shareholders and other stakeholders. But the bank disclosures are not available on internet in a timely fashion.

The bank also has an independent remuneration committee who creates compensation structure which is aligned with sound risk management and promotes long term health of the organization.

5.2 Recommendations

Banks' safety and soundness is the key to financial stability, and the manner in which they conduct their business, therefore, is central to economic health. The complexity of their operation and number of market participants who have a claim in it makes the governance of banks different from others. Governance weaknesses at banks that play a significant role in the financial system that can result in the transmission of problems across the banking sector and the economy as a whole.

Based on the survey the following points are suggested for the board of the bank and shareholders as recommendations for the existing problem.

- ❖ The board should manage to prepare a formal succession plan for the senior managers position since the future of the bank relies on the effectiveness of them. Senior managers should be formally selected trained and well prepared for their position before taking their place since they are the one who runs the bank closely and participates in the day to

day activity of the bank so the board of the bank has to prepare a well equipped senior manager while removing the other.

- ❖ The board of the bank should have sufficient information about the banks activity and needs sufficient time to acquire this information's since banks activity is bulky and complicated compared with other organizations and the success and failure of the bank is also depend on their effective governance quality. So the shareholders of the bank should make sure that board members have sufficient time to carry out their responsibilities and they have to ensure that members are ready to be a full time worker of the bank not as a part time job.
- ❖ Since board members are appointed to act on behalf of shareholders they have to act to fulfill the shareholders will not theirs so to remove such kind of problems shareholders of the bank have to appoint members who do not have economic as well as personal relationship to avoid any fevers and to maintain power balance between the members.
- ❖ All shareholders of the bank should have equal vote to BOD since all the decisions of the board affects all the shareholders majority as well as minority shareholders. Accordingly majority shareholders should give equal voting right to minority shareholders of the bank. As NBE directives indicate the banks standing nomination committee also has to ensure that all shareholders get equal opportunity in nominating potential candidate for a seat on the board.
- ❖ The board should ensure that the risk management of the bank is independent. Independency of the risk committee is very crucial to carry out its responsibilities effectively without any influence since its main responsibility is keeping the bank safe from any material risk the committee should carry out its duties independently without any influence.
- ❖ Disclosure is essential for sound and effective corporate governance. As set out in existing Basel Committee guidance on bank disclosure, it is difficult for shareholders, other stakeholders and market participants to effectively monitor and properly hold accountable the board of directors and senior management when there is a lack of information. To ensure disclosure of its material information, therefore, the bank's annual report should disclose the activities of each of the board committees and explain the incentive structure and remuneration practices for senior management, as well as the

actual amounts paid to senior managers and to directors this is also should be sited on the internet in the official site of the bank in a timely fashion.

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APPENDIX A

Questionnaire to be field by the Board members and senior managers of Dashen Bank

Dear Respondent,

This questionnaire is designed to gather data on “assessment on the application of corporate governance principles in the Ethiopian privet commercial banks, the case of Dashen Bank. The data to be collected through the questionnaire is highly valuable to meet the objectives of this study. Therefore, you are kindly requested to fill in and return the questionnaire. The information you supply would be used for academic purpose only and will be kept confidential.

Thank you in advance,

I. General information about the respondents

The following questions concern about your personal information. Completion of this Information is voluntary and its confidentiality is assured. No individual data will be reported.

1. Your sex, ☐ Male ☐ Female
2. Your marital status, ☐ married ☐ single other _____
3. Your age group, ☐ under 30 ☐ 30 to 45 ☐ 45 to 60
☐ 60 or older
4. Your highest level of education, ☐ diploma ☐ degree ☐ masters degree
☐ PhD ☐ other
5. Your work experience _____

II. Questions about the corporate governance principles

General guide lines

- Put a tick (✓) sign to appropriate space of particular score, which is suitable to your agreement about the following statements.
- The range scores are 1 for strongly disagree, 2 for disagree, 3 for undecided, 4 for agree, and 5 for strongly agree with the statement.

1.The roles and responsibility of BOD

No.	Roles and responsibilities	1	2	3	4	5
1	The BOD approves the banks strategic plan.					
2	The BOD monitors the implementation of the Strategic Plan					
3	The BOD oversees implementation of the appropriate governance framework.					
4	The BOD adheres to corporate culture.					
5	BOD monitors the senior management actions.					
6	The board ensures that appropriate succession plan is in place for senior management position.					
7	The board continuously ensures the skills of internal audit.					

2. Qualification and composition of BOD.

No	Items	1	2	3	4	5
1	The board members have sufficient knowledge in relevant areas.					
2	The board members have sufficient experience in relevant areas.					
3	The board has sufficient time to fully carryout their responsibilities.					
4	The board members do not have personal relationship with other members of the board.					
5	The board members do not have economic relationship with other members of the board.					

6	The shareholders ensure board members have access to ongoing training on relevant issues.					
7	The board comprises the minimum number of required independent number of board members.					

3. Structure and practices.

No	Items	1	2	3	4	5
1	The board periodically reviews its structure.					
2	The chair of the board is non executive board member.					
3	There is a mechanism that minority shareholders vote to the BOD.					
4	There is a formal procedure for selecting board members.					

4. Risk management.

No	Items	1	2	3	4	5
1	The risk management of the bank is independent.					
2	The bank has an approved risk limit.					
3	The risk management continuously identifies the risk exposures of the bank.					

5. Audit.

No	Items	1	2	3	4	5
1	The bank establishes an independent internal audit system.					
2	The internal audit has direct access to the BOD.					
3	The report of internal auditors does not filtered by senior managers.					
4	The audit committee is made up of non executive directors.					

6. Disclosure.

No	Items	1	2	3	4	5
1	The bank discloses appropriate matters to shareholders.					
2	The bank discloses appropriate matters to other stakeholders.					
3	The bank periodically discloses its corporate governance code to shareholders.					
4	All disclosures with shareholders made available on internet in a timely fashion.					

7. Compensation.

No	Items	1	2	3	4	5
1	The banks compensation structure is aligned with sound risk management.					
2	The compensation structure promotes long term health of the organization.					
3	The banks remuneration committee is independent.					

APPENDIX B

School of Business and Public Administration

MBA Program (graduate student)

Interview questions with the Dashen Bank's Senior Manager and the board.

1. How does the BOD follow the senior manager's activity? -----

 2. How the bank does controls managers from using its resource to their personal use by manipulating their power to their own sake? -----

 3. Does the bank disclose its risk exposures to the public? -----

 4. Do you think the bank aligns the long-term interests of the employees with its long term interests?-----

 5. What can you say about the existing corporate governance culture of the bank? -----

-