



Board Characteristics and Earnings Per Share of Malaysian Islamic Banks

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ABSTRACT

Board characteristics of the corporate organization represent an important aspect of corporate monitoring. This study examined the effects of board size (BS), the size of shariah supervisory board SSB and shariah board members meeting on the earnings per share of the Malaysian Islamic banks. The study used data from sixteen (16) full-pledged Islamic banks in Malaysia for 6 year period (2010-2015). The study used pool ordinary least square to estimate the regression after satisfying post - estimation tests. The results reveal significance positive relationship between BS, shariah board meeting and EPS at 1% level of significance. On the other hand, a negative relationship was found between shariah BS and EPS. The negative relationship between SSB size and EPS could be due to non-disclosure of the minimum number of shariah board members by some banks.

Keywords: Board Characteristics, Islamic Banks, Malaysia

JEL Classifications: M40, M41, M48

1. INTRODUCTION

Earnings per share (EPS) refer to the percentage of a firms profit apportioned to each of the outstanding shares of common stock. The EPS serve as an important indicator for the profitability of a company. EPS is the most important measure of performance indicator reported by company managements to the shareholders, market and other interested parties (Jorgensen, et al. 2014). The high quarterly EPS encourage top executives management's results to huge stock repurchases to helped them manage stock prices of their respective companies (Lazonick, 2014). Generally, EPS is the amount of money every share of common stock would get if all of the company profits were shared to the shares outstanding at the year end. The question here is whether corporate governance variables measured by board size (BS), SBS and shariah board meetings impact on the EPS of Islamic banks in Malaysia.

Corporate Governance variables are regarded as global issues that attracted arguments among researchers, portfolio analysts and other actors in corporate administrations. The financial

scandals in the recent period are largely credited to the failure of those organizations in their governances practices and that have upset the hope of the investing public (Strier, 2005). Corporate governance CG involves all those process and procedures whether structured or unstructured; principle or rule based that guides how a corporate entity is administered and control. CG variables also involve both internal and external governance mechanisms that guide the direction of the company for maximum shareholders benefit. The board of directors represents an important mechanism for corporate control and responsible for the overall monitoring of the management. In addition to the board of directors, Islamic financial institutions IFIs including Islamic banks are mandated to have Shariah Supervisory Board SSB to ensure that, the operations of the company are in conformity with principles of shariah (Islamic law). Similarly, the SSB are required to conduct meetings regularly to review bank operations and to approve a new product that may be introduced by the bank.

However, there is a little theoretical effort on the relationship between these governance variables and performance of Islamic

banks, more importantly, earnings to shareholders. This study filled a gap in the literature by empirically examining the effect of BS, SBS and SBM meetings on EPS of Malaysian Islamic banks.

2. LITERATURE AND HYPOTHESES

There is large empirical literature on the relationship between BS and board meetings on the performance of conventional corporate organizations. Some of the studies established a significant positive relationship between the variables and firm value while others reported a negative relationship. For example, Linck et al. (2008) reported that average increase in the number of BS is positively and significantly related to firm value amongst sample firms in the US. Firm BS has positive and significant relationship with subsequent firm value (Alimehmeti and Paletta, 2014). Similarly, Johl et al. (2015) tested board characteristics and firm performance amongst listed firms in Malaysian firms. The study findings showed that BS is associated with firm performance and board diligence also frequency of members meetings has a significant influence on the firm performance. In addition, Hoque et al. (2013) studied the frequency of company board meetings on the financial performance of firms in Australia. The findings of the study revealed a positive and significant relationship between the board frequencies of meetings and performance measured by return on asset and return on equity. On the contrary, Guest (2009) established that BS has significant negative impact on the Tobin's q and share return of the UK firms. BS has no significant association with the firm value measured by EPS (Gherghina, 2015). The theoretical background of this study is the agency theory; the theory explains the relationships which exist between principals (capital providers) and agents (managements). The theory designed to provide answers to the principal-agent problem. To achieve the objective of the study, the following hypotheses are tested.

- H₁: BS has a positive relationship with EPS of Malaysian Islamic banks
 H₂: Shariah supervisory BS has a positive relationship with EPS of Malaysian Islamic banks
 H₃: Shariah supervisory board meetings has a positive relationship with EPS of Malaysian Islamic banks.

3. METHODOLOGY

The study used secondary data from the published annual reports of the sixteen (16) Islamic banks in Malaysia. The data are collected on the individual bank basis for the period of six (6) years (2010-2015). The research utilized pool ordinary least square to estimate the regression and the post estimation test of normality, homoscedasticity, specification test and multicollinearity are satisfied.

3.1. Model Specification

$$EPS_{it} = \beta_0 + \beta_1 BS_{it} + \beta_2 SBS_{it} + \beta_3 SBM_{it} + \beta_4 LTA_{it} + \varepsilon_{it}$$

Where EPS = Earnings per share of banks over the period, BS = Board size, SBS = Shariah BS, SBM = Shariah board meetings and LTA = Natural log of total asset and ε is the error term for variables not captured in the model (Table 1).

4. RESULTS AND DISCUSSIONS OF FINDINGS

The descriptive statistic results revealed a mean and standard deviation SD values of 3.3,80,454 and 1.1,47,723 for EPS, 8.1,26,582 and 2.1,50,534 for BSIZE, 4.75,641 and 1.7,66,837 for SBSIZE, 8.7,54,098 and 4.6,49,931 for SBMEET and 3.3,79,871 and 0.94,65,095 for a log of total assets respectively. The minimum BSIZE is 3 and a maximum of 13, SBSIZE has a minimum of 0 and maximum of 9 due some banks under the sample failure to disclose their shariah board. The SD values clustered around the mean suggesting the normality of the data set (Table 2).

The correlation matrix table revealed a positive correlation of 0.2505 for BSIZE, the negative correlation of 0.3462 for SBSIZE, positive correlation of 0.0179 for SBMEET and positive correlation of 0.0034 for LTASSET and EPS Malaysian Islamic banks. The variable with the highest correlation is SBMEET and SBSIZE with a value of 0.5545 suggesting absence of multicollinearity in the model (Table 3).

The regression result presents a positive coefficient of 0.21,40,623 between BS and EPS of Malaysian Islamic banks (Table 4). This means that for every increase in BS from an average of 8 the EPS will increase by 0.2140623 Malaysian Ringgit (MYR).

Table 1: Variable definition and measurement

EVM variables	Measurements
EPS	Net profit less preference dividend divide by common stock
BS	Total number of board members serving in the bank
SBS	Total number of number of shariah supervisory board members in the bank
Shariah board members meeting (SBM)	Total number of meetings held by shariah committee members in the year
Total asset	Natural log of total asset

SBS: Shariah board size, BS: Board size, EPS: Earnings per share

Table 2: Descriptive statistics

Variable	Mean±SD	Minimum	Maximum
EPS	3.3,80,454±1.1,47,723	-0.94,16,085	5.6,53,541
BSIZE	8.1,26,582±2.1,50,534	3	13
SBSIZE	4.75641±1.7,66,837	0	9
SBMEET	8.7,54,098±4.6,49,931	0	21
LTASSET	3.3,79,871±0.94,65,095	1.2,32,333	4.3,69,448

EPS: Earnings per share, BS: Board size, SSBS: Shariah supervisory board size, SBM: Shariah board meetings, LTA: Natural log of total asset, ε : Error term for variables not captured in the model

Table 3: Correlation matrix results

Variable	EPS	BSIZE	SBSIZE	SBMEET	LTASSET
EPS	1.0000				
BSIZE	0.2505***	1.0000			
SBSIZE	-0.3462***	0.0361	1.0000		
SBMEET	0.0179***	-0.2509	0.5545	1.0000	
LTASSET	0.0034	-0.2039	-0.3083	-0.1084	1.0000

***Significant at 1% level of significance

Table 4: Regression results

Variable	Coefficient	T-value	P
BSIZE	0.21,40,623	3.12***	0.00
SBSIZE	-0.43,02,993	-4.33***	0.00
SBMEET	0.10,73,845	2.91***	0.00
LTASSET	-0.05,80,726	-0.28	0.783
Cons	3.1,53,489	2.71	0.009
R ²	0.3099		
Adjusted R ²	0.2472		
P-Chi	0.00		

***Significance at 1%

The probability of BS to EPS is 0.00 indicating a positive and significant relationship between the variables. The interpretation is that BS impacts positively to the EPS of the shareholders at the 1% level of significance. This provides a convincing evidence of accepting the study hypothesis which predicts a positive relationship BS and EPS of Malaysian Islamic banks. The result conforms to study of Johl et al. (2015) and contradicts Gherghina, 2015. Similarly, the result shows a negative coefficient of -.4302993 between SSB size and EPS of Malaysian Islamic banks. This suggests that an increase in SBS from an average of 4 the EPS will decrease by 0.2140623 MYR. The probability of SSB to EPS is 0.00 indicating a negative and significant relationship between the variables. The interpretation is that SSB size impacts negatively to EPS of shareholders at 1% level of significance. This provides a convincing evidence of rejecting the hypothesis which predicts a positive relationship SSB size and EPS of Malaysian Islamic banks. The possible reason why the negative relationship was found between SSB size and EPS may be due to violation of some banks under the sample to disclose minimum SBS of three (3) in their annual report. In fact, some of the banks did not disclose their SSB members. On the shariah board meeting the result reveals a positive coefficient of 0.10,73,845 between SSB meetings and EPS of Malaysian Islamic banks. This means that for every increase in board meeting from an average of 8 the EPS of Islamic banks will increase by 0.10,73,845 MYR. The probability of SSB meeting to EPS is 0.01 indicating a positive and significant relationship between the explained and the explanatory variables. The interpretation is that SSB meetings impact positively to the EPS of the shareholders at the 1% level of significance. This provides a substantial evidence for accepting the hypothesis of the study which predicts a positive association between SSB meetings and EPS of Malaysian Islamic banks. The findings supported Hoque et al. (2013). On the overall, the R² is 31% suggesting that 31% of the variation in the EPS is explained by the 3 CG variables

and 69% by other factors not captured in the model. The combined probability is statistically significant at 1% level of significance.

5. CONCLUDING REMARK

This study empirically examined the influence of BS, shariah supervisory board and shariah board meetings on the EPS of Malaysian Islamic banks. The study established a positive and significant relationship between BS and shariah board meetings of Islamic banks and EPS. However, the SBS was negatively related to EPS of the banks. This could be due to failure of some banks to comply with disclosure of minimum number of shariah board members as required by Bank Negara Malaysia. The study, therefore, recommends more vigilance to Islamic banks to ensure adherence to the regulatory guidelines. The 3 CG variables explained 31% of the variation in the EPS of Malaysian Islamic banks while the remaining 69% are explained by other factors.

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