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Corporate Governance of Egyptian State-Owned Banks

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ABSTRACT

Purpose: The purpose of this paper is to enhance understanding of corporate governance (CG) in) in the banking sector. It is devoted specifically to explore CG mechanisms adopted by the Egyptian State-Owned Banks (SOBs), including CG regimes forced by the law (Board of Directors, Auditors, Audit Committee and Credit Committee) and other CG modes adopted voluntarily by these banks.

Design/Methodology/Approach: The paper demonstrates models of CG and the mechanisms used in the banking sector. An exploratory research used to conduct a detailed analysis of Egyptian state-owned banks' CG mechanisms provided by banks' annual reports of 205l16 and other materials. In addition to reviewing all available documentation materials, including Egyptian Central Bank' publications and related documentations highlighting CG in the banking sector such as the Law No.88 of 2003 and The code of CG in Egypt of 2010. The paper conducts few in-depth interviews with key contacts in the three banks on the compliance to CG standards. Use of multiple-informants, including archival data and in depth interviews helped in crosschecking relevant information and verifying the reliability of data.

Findings: This paper reflects that most of the CG mechanisms used by banks are the ones imposed by laws and regulations, where they have a Board of Directors (BoD), an auditor and an audit committee. However, there are other committees voluntarily formed to improve CG, such as human resources committee, nomination and remuneration committees, and risk management committee. The board scope of power, the board full responsibility for CG, the board appointment by decree of Prime Minister after consulting with governor of the Central Bank of Egypt, and the board size and composition at SOBs in Egypt are increasingly adopting a more independent board of directors. The dominance of Non-Executive Directors (NEDs) on board committees is also found to enhance the adoption of board independence and the effectiveness of CG. This paper suggests the importance of internal CG mechanisms vis-à-vis external norms in the banking sector.

Research Limitations/Implications: The paper presents CG perspective in the banking sector through focusing on exploring CG norms used by SOBs in Egypt. This paper suggests new avenues of future research

for institutional perspectives of CG by suggesting CG mechanisms in banks is only part of the overall picture covering important fundamental systems.

Originality/Value: The paper provides a comprehensive study to help understand key CG mechanisms used by banks and provides theoretical implications to fill the gaps regarding CG in developing countries in general and in the banking sector in particular. The paper offers insights for policy makers interested in enhancing the efficacy of corporate governance regimes in the banking sector.

Keywords: Corporate Governance, CG Mechanisms, Board of Directors, Audit Committee, Auditors, Executive Committee, Egyptian State-Owned Banks, Egypt.

1. INTRODUCTION

As per the Organization on Economic Co-Operation and Development (OECD), CG is a set of relationships between different stakeholders, including a company's management, the board of directors, its shareholders and other stakeholders (OECD, 2004). This relationship must be based on trust and credibility in order to be sustainable. The final objective of the shareholders is to have appropriate return on their investments. Therefore, they must ensure that management is acting in accordance with their best interests since it is managing their own investments and is in some ways responsible for making suitable returns. Shareholders' interests may differ from those of other stakeholders, especially on risk tolerance (Mehran et. al. 2011). At the micro level, good CG motivates corporations' management to pursue the companies' objectives, facilitates monitoring and controlling the companies' activities and operations. While, at the macro level, effective CG structures provide a level of confidence necessary in the market economy (OECD [1]). Based on the importance of this theme, the literature review includes a diversity of studies on CG, including qualitative, quantitative, theoretical and empirical studies (Manolescu et. al. 2011).

The shareholders model, developed by Jensen and Meckling (1976), addresses the conflict of interests between a company's management and its owners. Particularly, the separation between management and ownership can create a conflict of interest between managers and owners, since the former will be a self-interest optimizer, acting to maximize their benefits and/or minimize their risk at the expense of owners (Jensen and Meckling, 1976; Shleifer and Vishny, 1986). To lower these agency problems, several CG mechanisms can be used. The ultimate goal of CG is to enhance the company's economic efficiency and strengthen its growth, provide a structure for setting objectives that will achieve the interests of the shareholders and other stakeholders, and determine the mechanisms that can be used to meet these objectives and manage their accomplishment (OECD, 2004).

Good governance is central to all stakeholders, particularly, shareholders. CG is related to the controlling of the activity. While controlling of the corporate sector can be termed as CG. But the implementation of CG is not that much simple as it may appear. It is very broad theme and it comprises much debate. No doubt CG is recently emerged concept and has taken the attention of countries, companies and managers, but its needs are in urgent state. CG is the practice that requires transparency, accountability and good performance from the corporate managers. It has its strong base from companies' management to the shareholders' value, as well as corporate social responsibility (Mehta and Chandani, 2013; Alshannag, Basah, & Khairi, 2017).

Enterprises take different forms across different countries and economies, and therefore it is difficult to develop a uniform thinking on the theme of CG accordingly. The literature review on banks' corporate

governance has been given less attention and has not been sufficiently considered despite its importance. Additionally, the recent global financial and banking crises have revealed the importance of enhancing understanding of bank governance (Pathan and Skully, 2010). The contribution of banks is central to any economy (Anwar & Sidin, 2016; Ahmad & Mazlan, 2015). They acquire publics' savings in the form of deposits, provide means of payment for goods and services and finance the development of businesses. Accordingly, banks' corporate governance concern not only shareholders and managers, but also customers, depositors and creditors. Therefore, banking governance is viewed by some authors as a public interest ((Macey and O'Hara, 2003; Damak, 2013).

In this context, this study is concerned with CG in the banking sector in Egypt, which may due to three considerations:

- The central role of banks in any economy; they obtain publics' savings in the form of deposits, provide payment methods for goods and services and finance the development of businesses. Therefore, banks' CG concerns customers, depositors, creditors and the community, not only shareholders and managers. Hence, banking corporate governance is recognized by some authors as a public interest (Damak, 2013).
- Unlike other business sectors and industries, the banking sector is characterized by the complexity of the operations, which increases information asymmetry and decreases the stakeholders' ability to monitor bank managers' decisions. These features of the banking sector require effective CG structures and the execution of more specific and complex banking CG mechanisms (Ţurleai et. al. 2010).
- The banking sector is highly regulated compared with other industries, due to its responsibility for protecting depositors' rights, ensuring the stability of the payment systems and lowering risk. Therefore, it is important to explore CG mechanisms used by SOBs in Egypt and to verify if these mechanisms forced by laws and regulations or voluntarily employed by banks.

In general, this paper explores CG structures in Egyptian banks. In particular, it examines CG mechanisms as stated by academics and practitioners, including ownership structure, board of directors, board characteristics, and board committees. Our goal is to provide useful information and a framework for thinking about the CG of banks. The paper is structured around seven sections. Section one demonstrates the conceptual background of CG, including agency problems, CG definitions, and CG mechanisms. Section two is concerned with reviewing the literature on CG on banks. Section three is concerned with highlighting research problem, research methodology and research limitations. The regulatory outlines of the Egyptian banking sector are addressed in section four. CG mechanisms adopted by SOBs in Egypt, including ownership characteristics, board of directors' characteristics and board committees' composition, roles and responsibilities are examined in section five. Finally, research conclusion is revealed in section six. The paper lasts with identifying some main policy and research issues that require further study on CG in section seven.

2. CONCEPTUAL BACKGROUND OF CORPORATE GOVERNANCE

This section tackles agency problems and CG models and demonstrates several definitions of CG from different perspectives. Also, the internal and external CG mechanisms are highlighted in this section. As per

Shleifer and Vishney (1997), the agency theory or shareholders model of CG focuses on how to motivate managers to act in accordance with the best interests of shareholders. In most countries, companies' managers are legally responsible to the shareholders. Hence, the difference between the legal rights of shareholders and the actual control of managers led to the development of shareholders model of CG (Jensen and Meckling, 1976); Fama and Jensen, 1983a,b); Hart, 1995). However, there are other models addressing the possibility of aligning the interests of managers, owners, and others.

2.1. When Agency Problems Arise?

The separation between ownership and control can create agency problems, due to the conflict of interests between companies' owners and managers (Rachagan and Satkunasingam, 2009). Several factors enable managers to optimize their own benefits; particularly they are better informed than owners about the activity of the business, and therefore opportunistic behavior can be practiced. Opportunism of managers can be done by handling private information and choosing the projects that create a maximum of the short term profits. Also, managers may take advantage from the lack of transparency to deliver only information that serves their interests. Hence, managers can preserve their positions from the competition in the labor market. In this context, (Stieglitz and Edling, 1992) propose a model through which managers enhance the investments of the company to increase information asymmetry. Similarly, (Morck et. al. 1990) indicated that the manager involves companies in several acquisitions to increase their own personal benefits, including acquisitions that generate negative consequences for the companies.

There are several agency problems can arise in companies. The first includes the conflict of interests between companies' managers and owners as indicated above. The second agency problem expands to include the conflict of interests between the majority or controlling shareholders and the minority or non-controlling shareholders. In this case, the non-controlling shareholders are the principals and the controlling shareholders are the agents, and the problem is to ensure that the controlling shareholders are acting in the best interests of the non-controlling shareholders. The third agency problem includes the conflict of interests between a company's management and the other stakeholders who have interests in or impact on the company, such as creditors, employees, customers and others. In this context, the problem is to assure that the management as an agent achieves the best interests of these other principals ((Rachagan and Satkunasingam, 2009). Also, agency problems can take the forms of adverse selection and moral hazard. Adverse selection arises when the principal employs an agent who is less competent, committed, productive, or ethical. Moral hazard can arise due to the lack of effort on the part of agents after hiring them. This risk can take different forms, such as commission or omission of actions and the consumption of advantages ((Rachagan and Satkunasingam, 2009)). This paper addresses the agency problem which arises from the conflict of interests between managers and owners.

CG includes the legal, institutional, and cultural mechanisms, which allow shareholders to lower agency problems (John and Senbet, 1998); Peace and Osmond, 1999). Good CG therefore plays a central role to solving these agency problems by enabling shareholders to exercise control over corporate executives, align the interests of these groups and lead to superior performance (Jensen and Meckling, 1976; Fama and Jensen, 1983b; Daily and Dalton, 1994). CG mechanisms, including internal and external norms should be adopted in order to align the interests of agents and principals (Bozec and Bozec, 2007).

According to literature review, there are several CG models have been developed, including the shareholder model, which ensure the interests of the shareholders (as described above). The second, the stakeholder's model, which recognizes the interests of employees, managers, suppliers, customers and the community. The stakeholder model argues that managers are not only responsible for satisfying shareholders' motives, but also for acting in the best interests of a broad range of stakeholders, including employees, customers, suppliers, creditors, depositors and the community as whole. Therefore, managers should act in accordance with stakeholders' interests in order to ensure their rights and their participation in decision making and must act as the stockholder's agent to ensure the survival of the company to maintain the long term stakes of each group (Fontaine et. al. 2006).

The third model is the stewardship model which claims that the conflict of interests between managers and owners can be avoided (Jeffers, 2005; Donker and Zahir, 2005; Letza et. al. 2008). This model argues that managers or agents are not motivated by opportunistic interests but rather they are stewards and behave in the best interests of shareholders or principals. Unlike the shareholder model, which claims that conflict of interest between managers and shareholders is inevitable unless appropriate CG mechanisms are employed to align the interests of managers and owners (Jensen and Meckling, 1976). The stewardship model indicates that stewards (managers) will be satisfied and motivated when institutional success is attained even at the expense of their own individual motives. Furthermore, while the shareholder model claims that shareholders' interests will be protected by avoiding board duality, the stewardship model argues that shareholder interests will be maximized by appointing the same person to the two posts to provide more responsibility and autonomy to the CEO as a steward in the company (Donaldson and Davis, 1991).

2.2. Corporate Governance Definitions

CG can be perceived from different perspectives (Van den Berghe and Carchon, 2002); Sison, 2008). Firstly, CG can be viewed at the level of the board of directors; secondly, it can be viewed at the level of the so-called *"corporate governance tripod"* comprising shareholders, directors and management; thirdly, CG can be viewed from the perspective of a company's direct stakeholders, including employees, suppliers and customers; fourthly, from the viewpoint of a company's indirect stakeholders, including the government, the environment and the society as a whole. Finally, CG can be understood from a global perspective that considers the economic, legal and cultural environments in which an organization works and competes in (Ţurleai et. al. 2010).

Diverse CG definitions reflect different conceptual frameworks or models. For instance, the definitions that are articulated by Cadbury (1992); Shleifer and Vishny (1997), such as "*CG is the system by which companies are directed and controlled"* indicated that CG is associated with both ownership and control, and targeted to maximize shareholders' interests. Alternatively, the definitions of (OECD, 2004; Sison, 2008; Solomon, 2010) are directed by the stakeholder model, which outlines the rights and responsibilities of each major group of stakeholders in a company (Shahin and Zairi, 2007). For example, *"CG is the system of checks and balances, both internal and external to companies, which pushes companies fulfilling their accountability to all stakeholders and act in a socially accepted manner*" is associated with the stakeholder model Sison [28]).CG can be defined as the "set of relationships between a company's management, its board, its shareholders and other stakeholder". They emphasize the importance of attaining and ensuring justice and equality to all stakeholders through transparency and accountability (Ghayad, 2008; Magalha and Al-Saad, 2013; Lewis, 2007). This study

adopts the definitions that reflect the shareholders model, particularly the Cadbury definition of CG as: "a system by which companies are directed and controlled", which highlights the main players' roles in an organization, including shareholders, the board of directors as well as the auditor (Cadbury, 1992).

2.3. Corporate Governance Mechanisms

CG mechanisms can be defined as a set of control structures or norms used by shareholders to align their own interests with managers' interests and to monitor and control managers. The purpose of these CG mechanisms is to limit the scope and frequency of agency problems and to ensure that agents act in accordance with the best interests of their principals (Hill and Jones, 2009). There are two distinct types of CG mechanisms: internal and external mechanisms (Hill and Jones, 2009; Damak, 2013):

2.3.1. Internal Corporate Governance Mechanisms

Internal CG mechanisms are the internal norms used by companies which can persuade managers to maximize the shareholders' value. These tools include, board of directors, audit committees, auditors, ownership structures and stock-based compensation methods.

(A) **The Board of Directors (BoD):** It is the basis of the CG system in companies worldwide. The board members are directly elected by shareholders to represent shareholders' interests. Hence, the BoD is responsible for monitoring corporate strategy decisions and controlling management activities, ensuring that managers pursue strategies that are in the best interests of stockholders. In addition, the BoD is legally accountable for the company's actions and is authorized to hire, fire, and compensate corporate executives, including the CEO. Furthermore, the BoD is responsible for the verification of financial reliability and compliance with laws and regulations and the reduction of information asymmetry between owners and managers (Hill and Jones, 2009). The typical BoD comprises a mixture of Executive Directors (EDs) and Non-Executive Directors (NEDs). EDs are required on the board because of their valuable information about the company's activities. While, NEDs are needed to bring objectivity to the monitoring and evaluation processes, particularly their needs to maintain a reputation as independent directors gives them an incentive to conduct their tasks as professionally as possible (Fama and Jensen, 1983a).

(B) **Board Committees:** Committees are complementary components to the BoD. They are required to conduct specific activities or tasks that are delegated by the board. Board committees can be formed by the laws and regulations and can be recommended by the board depending on nature of business sectors in which companies work and compete. The number and structure of the committees that are created by laws and regulations vary from a country to another. However, committees which most commonly provided are: the audit committee; the nomination committee, the executive committee and the remuneration committee.

(C) **Financial Statements and Auditors:** Public stock companies (PSCs) in most countries are required to reveal quarterly and annual reports aiming to provide consistent, detailed, and accurate information about how efficiently and effectively the agents are managing the company. This financial information must be audited by an external auditor, in order for shareholders to

ensure that the information contained in financial statements accurately reflects the company's financial position (Hill and Jones, 2009).The role of the auditor is to provide shareholders with more developed and relevant information. The internal audit function plays a central role to the ongoing assessment of a bank's internal control, risk management and governance systems and processes–areas in which supervisory authorities have a keen interest (Damak, 2013).

(D) **Ownership Structure:** it is a tool to control the relations between shareholders and managers. The ownership structure provides the basis for efficient monitoring system, namely. As per the shareholders model, two components of the ownership structure, the concentration of capital and the nature of the shareholders may be the cause of the performance of a company.

(E) **Stock-Based Compensation:** As per the shareholders model, one of the most effective mechanisms to limit the scope of the agency problems is to motivate management to act in accordance with the best interests of shareholders through pay-for performance system. Where, shareholders can motivate top managers to pursue strategies that maximize a company's long term profitability and profit growth, and thus the stocks' value, by linking managers' pay to the stock price. The stock options grant managers the right to buy the company's shares at a predetermined price at some points in the future. This tool aims to motivate managers to pursue strategies that increase the shares' value (Hill and Jones, 2009).

2.3.2. External Corporate Governance Mechanisms

Given the limitations of internal CG mechanisms used by companies, there is another type of control that can contribute in managing the potential conflict of interests between shareholders and managers. This control is carried out by the market including: the financial market, the market of goods and services, and the labor market of managers.

(A) **The Financial Market:** The role of the financial market in controlling the company's management is becoming more important in economies in which there are developed stock markets. There is a positive relationship between efficiency of managers and the company's market value. If the management strategy is likely to endanger the advantages of shareholders, they can sell their shares. Hence, if they start doing so in large numbers, the value of the company's shares will decrease and may become an attractive acquisition target and runs the risk of being acquired by another company, against the wishes management. The takeover constraint limits the extent to which managers pursue strategies and take actions that achieve their own interests at the expense of their shareholders (Hill and Jones, 2009).

(B) **The Goods and Services Market:** Competition in the market of goods and services can endanger top managers who act in accordance with their own interests at the expense of shareholders' motives. In practice, any competitive market leads the managers to maximize the company's resources and to play a preventive role against the failure of the company. However, the effectiveness of this mechanism of control is limited (Damak, 2013).

(C) **The Labor Market for Managers:** The labor market is an effective control mechanism due to addressing the importance of human capital in management. Managers are constantly faced with the pressure of the labor market. This market allows for the selection of the most competent

managers based on their merit through the competition which exists between external and internal managers.

3. LITERATURE REVIEW ON CG IN THE BANKING SECTOR

Table 1
Finding of Previous Literature on CG in the Banking Sector

Authors	*Key Findings*
(Dalwai et. al. 2015)	This study reviewed literature on CG and its impact on firm performance in the Gulf Cooperation Council (GCC). It analyzed the different empirical and theoretical contributions in establishing the relationship between CG and bank performance. Findings revealed the need for more research studies on banks' CG in the GCC.
9Ţurleai et. al. 2010)	This study examined the characteristics of CG in the banking sector. It indicated that there is and it should be a relationship of complementarities between the main CG mechanisms, including internal audit, audit committee, and external audit.
(Aboagye and Otieku, 2010; Abraham et. al. 2008; Schachler et. al. 2010; Nathan and Ribière, 2007; Jamali et. al. 2007])	These studies examined the relationship between CG mechanisms and banks' performance, including the relationship between banks' CG practices and financial reporting process; the relationship between CG failure and financial problems in the banking sector etc. Findings indicated the uniqueness of the banking sector and the need for effective CG mechanisms to be used by banks.
(Al Saeed, 2013; Bawaneh, 2011; Abu Risheh and Al-Sa'eed, 2012)	These studies explored the degree of Jordanian banks' compliance with the OECD's principles of CG. Findings revealed that the banking sector in Jordan comply with the OECD corporate governance principles. Also, results found that banks comply with CG requirements by acting in accordance with Jordan Central Bank CG guidelines and requirements which are driven from OECD principles of CG.
(Ţurleai et. al. 2010)	The study investigated the impact of the disclosure on CG in major Australian banks. Findings indicated the subjectivity of financial reports issued by these banks and the inability of these reports to present an accurate overall picture of reality.
(Fanta et. al. 2013)	The study investigated the influence of internal and external CG mechanisms on bank performance as measured by return on equity (ROE) and return on assets (ROA). Results revealed that there is a significant positive relationship between bank size and capital adequacy ratio and bank performance. While there is a significant negative relationship between board size and board audit committee and bank performance.
(Al-Hawary, 2011)	This study investigated the impact of CG on Jordanian conventional banks' performance. Results indicated that there is a significant relationship between CEO duality of direction, board independence, ownership concentration, and capital adequacy on the one hand and bank performance on the other hand. While there was no a significant relationship between leverage and banks performance.
(Sunday, 2008)	This study examined the relationship between CG and Nigerian banks' performance. Findings found that the duality of direction and bank performance are positive associated. .
(Tandelilin et. al. 2007)	The study examined the relationship between CG, risk management, and bank performance in Indonesian banks. Findings revealed that risk management had significant effect on bank performance, and the relationship between CG and bank performance is affected by the type of bank ownership.
(Kim and Rasiah, 2010)	The study examined the impact of CG on bank performance in Malaysia. Findings indicated that foreign banks had better CG practices than domestic ones.

Authors	*Key Findings*
(Sunday, 2008; Dallas, 2004)	These studies examined the impact of board characteristics (board size, independence, activity, and remuneration) on banks' performance. Results revealed that board size can be an important governance consideration and the optimal size of the board should be established for good CG as well as firm performance.
(Inam and Mukhtar, 2014)	This study investigated the impact of CG on banks' performance in Pakistan. Results indicated that good CG is significantly associated with better bank performance.
(Toufik, 2015)	This study explored the main elements of CG in Islamic Banks (IBs), including the role played by Shari'ah Supervisory Board (SSB). Results revealed that IBs are progressing in adapting CG structures, such as accountability, transparency and trustworthiness and the SSB is playing a central role to IBs in terms of effective advisory and counseling.
(Daryaei et. al. 2013)	This study explored CG in IBs, by comparing CG structures with Islamic values. Results revealed that developing without regard to economic systems and culture is impossible, because economic systems and culture are associated. Also, it indicated that the aligning principles of western CG with Islamic values as accountability, transparency, social justice and trustworthiness, help companies to attract investment and improve their performance.
(Ghaffar et. al. 2014)	The study investigated the impact of CG mechanisms adopted by IBs in Pakistan on bank profitability measured by ROA and ROE. Results revealed that the profitability of IBs in Pakistan tends to increase with the adoption of good CG practices.
(Grassa and Matoussi, 2014)	This study investigated the current CG practices and structures of IBs in the GCC and Southeast Asia. Results indicated that there were significant differences of CG structures of IBs in GCC countries and those in Southeast Asia countries (Malaysia and Indonesia).
(Al-Beshtawi et. al. 2014)	This study explored the role of CG in Jordanian's conventional and Islamic banks and its impact on financial and non-financial performance indicators. Results revealed that both apply principles and components of CG. Also, findings indicated the need for greater attention to the competent authorities to monitor financial and non-financial performance of Jordanian banks and increase the provisions of the law and the legislation imposed by the government and the competent application of CG.
(Garas, 2012)	This study explored the conflict of interests in the Sharia 'a board and the conflict of interest between the Sharia 'a board and board of directors and other third parties in IBs. Findings indicated that the conflict of interests in the Sharia 'a board is significantly affected by the executive position of the Sharia 'a board members.
(Grassa and Matoussi, 2014)	This study examined whether a multi-layer CG model instituted by the Islamic banking system offers protection against its weakness to financial crises. Findings found that the CG model followed by IBs provides better protection against crisis.
(Grassa et. al. 2010)	This study examined the impact of the Sharia 'a board on financial and ethical performance of IBs. Results indicated that there was no significant relation between financial performance and Sharia 'board characteristics.
(Touny, 2014)	This paper examined the macroeconomic determinants of the banking sector development in Egypt and Saudi Arabia (economic growth, financial liberalization, trade openness, economic globalization and monetary policies). The study revealed that economic growth has a long-term negative impact, while financial liberalization and real interest rate have significant positive impact on credit to the private sector in both Egypt and Saudi Arabia. Furthermore, trade openness has a positive impact on the credit to the private sector in Egypt
(Zerban and Ateia, 2016)	The study explored the effect of separation the positions of Chief Executive Officer (CEO) and Chairman of the board of directors on the financial performance of banks in Egypt. It measured financial performance by ROA and ROE since both ratios summarize the final results of the bank performance. Results revealed that there is no a full separation between chairman and CEO positions in some Egyptian banks.

Authors	*Key Findings*
(Mubarak, 2011a)	This study examined three hypotheses about disclosure of accounting information of banks and effects on quality of information in Egypt and the UAE after the global financial crisis. By analyzing data for years (2003-2005) as representative of pre-crisis and (2009-2011) as post-crisis. The findings revealed that there was more disclosure about financial items, operations abroad, directors and their remuneration in both countries after the crisis than before and in the UAE more than in Egypt. It was also a positive association between disclosure and quality of information in terms of the timeliness and credibility it covers.
(Banerjee et. al. 2010; Sami et. al.2007))	These studies analyzed the compliance of HPCs as well as ORDs with good corporate governance measures. Results indicated that HPCs scored higher measures of CG than ORDs, however the results did not strongly support that Indian HPCs apply superior corporate governance practices. They also found that CG measures are positively and significantly associated with company performance and valuation.
(Sánchez, 2013)	This study examined the effectiveness of Spanish corporate governance by analyzing the impact of board characteristics, including board size, board independence, board reputation, board diversity and board activity on efficiency. Results indicated that business efficiency is associated with heterogeneous boards with a limited number of directorships per director and with a limited activity specified in a reduced number of annual board meetings with a higher number of specialized committees.
(Al-Malkawi and Pillai, 2010)	This study investigated the relationship between internal corporate governance mechanisms and company performance. Results revealed that the smaller board size, non-existence of duality and favorable dividend mechanisms are effective internal governance mechanisms affecting company performance. Also, results found that there is no evidence on the relationship between leverage and institutional ownership as internal governance mechanisms influencing agency cost and company performance.
Mehta and Chandani [2013)	This study investigated Indian corporate practices in terms of CG with board of directors' parameters and evaluated the same with the international board. Results emphasized the governance pattern among Indian corporate sector.

4. RESEARCH PROBLEM AND METHODOLOGY

4.1. Research Problem

The role of CG is central to directing and controlling management strategies, policies, decisions and activities to achieve shareholders' interests. CG has been recognized as one of the main research themes that affect all types of companies and banks in particular. Despite the importance of CG, empirical research in this area, particularly in the banking sector is still limited. This study aims to demonstrate the importance of CG particularly for financial institutions and explore the specific CG mechanisms used by SOBs in Egypt. The research problem is to explore the CG mechanisms adopted by Egyptian state-owned banks. This study therefore aims to examine empirically the existence of certain CG mechanisms in Egypt's banks. More specifically, this study seeks to address the following questions:

1. Which corporate governance mechanisms used by Egyptian state-owned banks either forced by the laws and regulations or used voluntarily by these banks.
2. To what degree banks' boards of directors in Egypt are independent.

4.2. Research Methodology

To tackle the above questions, an exploratory research used to conduct a detailed analysis of Egyptian state-owned banks' CG structures or norms provided by annual reports and other materials, together with a review of other relevant literature, particularly on CG in the banking sector in Egypt. More specifically, to explore the specific corporate governance mechanisms used by SOBs in Egypt that include those forced by the laws and others decided on voluntarily by these institutions. In addition to analyze the degree to which the participating banks' boards of directors are independent, annual reports of the participating banks have been investigated as the data source. Furthermore, All available documentation materials have been examined, including Egyptian Central Bank' publications and related documentations highlighting CG in Egyptian companies such as the Law number 88 of 2003 on the CBE, the Banking Sector and Money (2003) and the Law No. 159 of 1981 on Commercial Companies (1981).

Six in depth interviews have been conducted with board members in SOBs, covering all CG systems adopted by these banks, particularly the implementation of CG frameworks in their banks and the justification of board duality. The interviews provided much information on CG mechanisms used by the three banks and how these banks comply with CG standards and guidelines. Furthermore, the key contacts indicated how the CG plans and structures are put into reality and the significant role of the chairman of the board of directors who undertakes the duties and activities of the CEO as well. The use of multiple-informants, including in depth interviews and the use of archival data helped in crosschecking relevant information and verifying the reliability of data. For the purpose of the paper, all SOBs in Egypt in 2015/16 were studied. Alexandria bank was excluded from the study due to the transfer of the bank from government to private sector in 2007. Table 3 depicts the SOBs in Egypt subject to this study. The study involved the analysis of annual reports of the banks stated bellow for the years 2010 up to 2015. Additionally, other information has manually collected from annual reports and the websites of these banks. Furthermore, board members were also interviewed on CG mechanisms used by banks in general and on some specific issues such as relations with shareholders and board independence in particular.

Table 2
Investigated Egyptian State-Owned Banks in 2015/16
(Public Stock Companies-P.S.C)

NO.	*State-Owned Banks*	*Total Equity (Egypt's Pound-EGP)*
B1	National Bank of Egypt (NBE)	33.543 Billion
B2	Banque Du Caire (BDC)	6.065 billion
B3	Banque Misr (BM)	23.3 Billion

Source: Adapted from State-Owned Egyptian Banks' Annual Reports, 2015/2016.

4.3. Research Limitations

This study is limited to explore the existence and practice of CG mechanisms and the board independence of SOBs in Egypt. Hence, CG structures or norms are not investigated in Private and Joint Venture, Off-Shore and Specialized Banks (Industrial Bank, Real State Bank, Agricultural Bank) working in Egypt. In addition to, external governance mechanisms opted for by Egyptian state-owned banks are not examined due to the lack of information on these external mechanisms in most of banks' annual reports.

5. REFORMS AND REGULATORY OUTLINES OF THE EGYPTIAN BANKING SECTOR

The following section addresses the role and features of the banking sector and the CG guidelines for Egyptian banks.

5.1. Characteristics of the Banking Sector

The banking sector is central to the success of any economy. All industries and sectors in any economy are significantly affected by the banking sector. Loans from banks are the main source of external finance for companies in most of economies. Levine (2014) emphasizes the importance of banks for industrial expansion and capital allocation. The efficient allocation of funds by banks reduces the cost of capital to companies, enhances capital creation, and encourages productivity. Therefore, banks influence the effectiveness of companies' operations and the prosperity of nations.

Information asymmetry occurs in all industries, as Levine (2014) highlights, but it is greater with banks. Moreover, the lack of balance of a single bank can easily affect other banks and influence the whole banking sector, with negative effects for the whole economy and finally for the economic and political stability of a country. The banking sector is becoming increasingly global, the operations with corporate customers, as well as the operations with private customers that have recently become more and more regular. Other characteristics, including the crucial role in the payments system, the complexity, the trend to instability and the systemic risk confirm the existence and necessity of rigorous regulations of the banking sector. The functions of banks differ from those of other companies, and therefore banks are subject to strict regulations of their capital and risk. Moreover, these differences are reflected on CG practices used by the banking sector. The role of banks to protect depositors' funds has made corporate governance important for financial institutions to maintain public trust towards the banking system and to maintain the stakeholders' confidence including the shareholders and investors.

5.2. Developments and Reforms of the Banking Sector in Egypt

Egypt has made significant developments and reforms in the banking sector in order to raise the level of its performance and its role in the national economy. The banking system in Egypt has passed through several stages since the 1952 revolution up to the present time. The first stage after the revolution of 1952 to the beginning of the seventies of the last century showed the nationalization and the integration of banks operating in the country. This stage has led to the formation of large-sized banking. The second stage from 1974 to the beginning of 1980s has been characterized by the implementation of the open-door policy, where foreign banks were allowed to operate in Egypt and the degree of competition between banks has been increased accordingly (Touny, 2014).

The third stage during the 1980s has been characterized by amending some provisions of the Banking Law and credit, and enhancing the role of the central bank to tighten controls on banks. The fourth stage from 1990 until the mid of 1990s, the Egyptian government launched the stage of liberalization and economic reform, which led to liberalizing the interest rate and exchange rate and changing the mechanism of financing the budget deficit through treasury bills. The fifth stage since1997 until now, a number of policies and measures have been adopted to increase the role of the banking system in financing the investment and

make banks more able to cope with the market demand. For instance, the government has prepared an executive program aiming at reforming and recapitalization of banks, as well as the integrating the small entities to achieve an efficient application of the rules of financial control and supervision (Touny, 2014; Mubarak, 2011a). As per USAID/Egypt (2004) [70], the banking sector in Egypt implies 28 commercial banks, including four SOBs and 24 Private and Joint Venture Banks (JVBs). In addition to 34 non-commercial banks, including 31 business and investment banks and 3 specialized banks (whose main activities are, roughly the same as those of commercial banks). The 4 state-owned commercial banks-the National Bank of Egypt (NBE), the Bank of Alexandria, the Banque du Caire (BDC), and the Banque Misr (BM) dominate the sector due to their size in terms of assets, deposit base and branches (an average of 200 branches each), accounting for 55% of the banking system's total assets. The Central Bank of Egypt supervises all banks in Egypt except for Misr African International Bank, the Arab International Bank and the Egypt Export Development Bank (Mubarak, 2011a).

Table 3
The Banking Sector indicators in Egypt

US million Banking Activity	*2010*	*2011*	*2012*	*2013*	*2014*	*Nov. 2015*
Assets	221.047	216.740	226.556	242.209	275.375	320.636
Deposits	164.053	163.948	171.486	189.242	218.210	240.186
Credit Facilities	78.928	81.148	81.248	79.134	88.028	100.224
Capital + Reserves	13.794	13.530	15.834	16.296	17.174	17.917
Growth Rates (GR) in Assets	5.3%	–1.9	4.5	6.9	13.7	16.4
GR in Deposits	4.7%	–0.1%	4.6%	10.4%	15.3%	10.1%
GR in Credit Facilities	0.1%	2.8%	0.1%	–2.6%	11.2%	13.9%
GR in Capital + Reserves	19.1%	–1.9%	17.0%	2.9%	5.4%	4.3%
Capital to risk-weighted assets	–	15.9	14.9	13.7	13.0	–
Net worth to assets	–	6.8	7.2	7.1	6.9	–
Nonperforming loans to total loans	–	10.5	9.8	9.3	9.1	–
Return on assets	–	0.8	1.0	1.0	1.0	–
Return on Equity	–	11.7	13.9	14.5	14.5	–
Liquidity ratio	–	55.6	58.4	61.8	62.9	–
Loans to deposits	–	50.2	48.1	44.1	41.1	–

Source: adapted from:

– Central Bank of Egypt, Bank Audi's Group Research Development, February 24, 2016.
– IMF, Country Report No. 15/33, February, 2015.

The economic reform program launched by the government of Egypt in mid of 1990s incorporated different aspects, such as the elimination of the repressive measures that had been in practice since the early 1960s, the liberalization of loan and deposit rates in 1991, followed by the removal of ceilings on bank loans to the private sector in 1992. Also, service fees and bank charges were freed up; the reserve requirement ratio was reduced; and majority foreign ownership was permitted (Omran, 2003).With regard to the banking sector privatization, the government attempted to reduce market concentration and enhance competition; the Egyptian government launched an active bank privatization program in 1994. This program implied two separate dimensions, the privatization of joint venture banks and the privatization of state–owned

banks. In reality, the state has already sold its equities in 21 joint-venture banks, in addition to Bank of Alexandria (Ford, 2007; OECD, 2012).

The literature review suggests that CG mechanisms of banks require an empirical investigation to recognize and distinguish the different CG frameworks from those of other companies. The foregoing literature review on CG in banks has outlined that CG as an important agenda because it has an impact on the growth, employment and economic development of a country. This research focuses on corporate governance mechanisms adopted by Egyptian state-owned banks because their conduct and behavior can have the positive/negative impacts on the country economy.

5.3. CG Guidelines for the Banking Sector in Egypt

Egypt was a pioneer in the in the Middle East and North Africa (MENA) in developing domestic CG code, launched in 2005; it has been based on the OECD Principles of CG. The launch of the Egyptian Institute of Directors was as much a response to the existing demand for governance know-how, as it was to encourage a stronger application of CG. Koldertsova (2010) recognizes two waves of CG in the MENA region; the first was in 2005 and the second was in 2010. Such code was introduced as voluntary guidelines, providing best-practice recommendations based on international standards, notably the OECD Principles of CG and only recently, regulators attempted to introduce stricter requirements. In Egypt, board independence requirements first stipulated in the governance code were subsequently incorporated into the listing standards of the Egyptian Stock Exchange.

A survey in 2006 by the Egyptian Banking Institute about CG in Egyptian banks reported the following findings Mubarak (2011a):

- Banks have a good CG framework need to be better communicated.
- Banks have written policies regarding corporate governance and codes of ethics.
- Banks treatment shareholders equitably to a large extent..
- Banks have a high level of disclosure of financial information and transparency in line with international standards.
- More effort needs to be done in terms of designing and implementing special training programs on CG and internal control practice for employees.
- Banks have board committees for supervising and monitoring major business functions, including specialized committees concerned with good governance and risk management.
- Banks have EDs and NEDs on the banks' Boards.
- Banks do not consider the evaluation of clients' corporate governance practices in their credit risk assessment systems.

6. CG MECHANISMS IN EGYPTIAN STATE-OWNED BANKS

Statistics on CG mechanisms used by each bank in the study, particularly internal CG mechanisms are presented in the following tables. For reasons of clarity, the following tables firstly present the CG mechanisms and other relevant data of every bank in the study.

Table 4
CG Mechanisms Used By Egyptian State-Owned Banks

Governance Mechanisms	*NBE*	*BDC*	*BM*
The Board of Directors	X	X	X
The Executive Committee	X (EDs)	X (EDs)	X (EDs)
Audit Committee	X (3 NEDs)	X (3 NEDs)	X (3NEDs)
Human Resources Committee	X (6 EDs)		
Remuneration and Compensation Committee (Compensation and Benefits Committee)	X (3 NEDs)	X (3 NEDs)	X
Governance and Nomination Committee (Corporate Governance Committee)	X (3 NEDs)	X (3 NEDs)	X
Credit Committee (Senior Credit Committee)	X*	X*	X
Risk Management Committee (Higher Risk Committee)	X (4NEDs and 2 EDs)	X (2 NEDs) and 1 (EDs)	X
The auditor	X	X	X
Investment Policies Committee (Supreme Investment Committee)		X (2 NEDs and 1 EDs)	X
IT and Banking Technology Committee		X (3 NEDs)	X
Committee of Informatics			X
The Financial Market			
The Market for Goods and Services			
The Labor Market			

Source: Adapted from Egyptian State-Owned Banks' Annual Reports, 2015/2016.
X* Management Committee not Board committee

For good understanding and analyzing the information depicted by these tables, it is necessary to translate the information incorporated in Tables 4 and 5 in histograms which facilities the reading and understanding of the results and makes it more relevant to identify characteristics of the corporate governance structures of banks. CG mechanisms adopted by Egyptian State-Owned banks need to be enhanced by other information that have a direct impact on the banks' CG, including the ownership characteristics, the size of the board of directors, the percentage of NEDs on the board vis-à-vis EDs, and the case of dual direction, where the president of the board is him/herself the chief executive officer (CEO). This information provides a clear depiction of the independence of the board and therefore the effectiveness of its governance.

Table 5
Board Size, Independence and Ownership Structure of Egyptian State-Owned Banks

Measures/Stand.	*NBE*	*BDC*	*BM*
The Size of Board of Directors	8 [8]	10 [9-2]	8 [8]
Dual Direction	YES	YES	YES
The number of Non-Executive Directors on the Board of Directors	4	6	4
The number of Executive Directors on the Board of Directors	4	4 (3)	4

Measures/Stand.	*NBE*	*BDC*	*BM*
Directors on Appointment*	GA	GA	GA
Directors' Compensation*	GA	GA	GA
Board Performance Evaluation	Board	Board	Board
A total number of meetings during 2013	12	?	?
Ownership Structure (Government-Others**)	Fully owned by Government	Fully owned by BM (Government)	Fully owned by Government

*GA (General Assembly)
**Others (Private Companies and/or Individuals)
Source: Adapted from Egyptian State-Owned Banks' Annual Reports, 2015/2016.

6.1. Characteristics of Ownership

As per the shareholders model two components of the ownership structure, including ownership concentration and the nature of the shareholders may be the reason of the corporation performance. The ownership structure is considered to be an effective mechanism of control of management, when certain conditions are present, including capital concentration and nature of the shareholders (Fontaine et. al. 2006). As per the annual reports of SOBs in Egypt, the ownership of the three state-owned banks is concentrated in government hands. Moreover, the ownership of these banks is held by large government institutions. These highly concentrated ownership models in Egypt, like those found in Germany. Unlike, countries such as UK and USA with high levels of fragmented ownership, which tend to have stronger protections for minority shareholders and mandatory information disclosure requirements. (Williams and Mas, 2010).

The nature of shareholders is an additional way of monitoring the activities of management provided by institutional investors. For example, (Mcknight and Weir, 2009) indicate that institutional investors vote more actively on anti-takeover changes than do other shareholders, and that they are more likely not to accept suggestions that are not acting in the best interests of shareholders. Institutional investors have greater expertise and resources and can monitor management at lower costs than the average private shareholder. Large owners can be particularly important in corporate governance since not all owners are able and willing to control management, but assume that shareholders with large shares will monitor and control the management. More concentrated shareholdings provide a great incentive and ability to monitor management and control over the board of directors (Mcknight Weir, 2009; Bolton and Scharfstein, 1998). Hence, according to Gedajlovic and Shapiro (1998), concentrated ownership is a powerful constraint on managerial discretion.

Based on the ongoing argument, the motivation of shareholders to monitor the management activities is based on their equity stakes. Small or non-controlling shareholders have little or no motives to practice monitoring behavior, while, large or controlling shareholders have more incentives to control management (Shleifer and Vishny, 1997; Hart, 1995). In general, the bigger the number and amount of stocks that owners have, the stronger their motives to monitor and protect their investment. The large institutional investors play a crucial role in corporate monitoring and protecting the interests of minority or non-controlling shareholders. In USA, the large institutions play a central role in pursuing greater board independence and in choosing the lead directors for chairman post in companies in which they invest their fund (Hashim and Devi, 2004). Gillan (2006)) indicated that institutions that hold large equity stakes in a company are

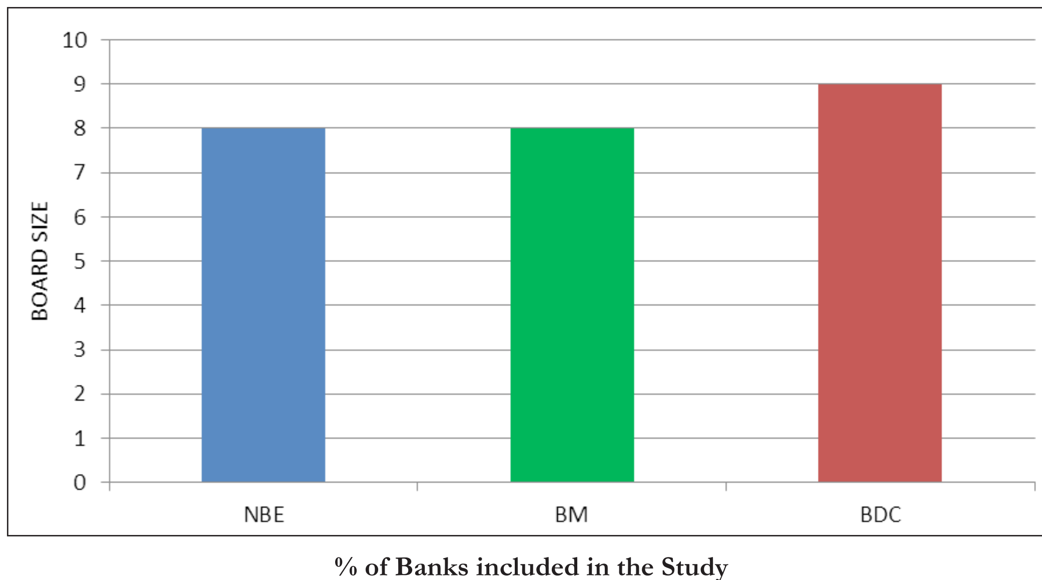
involved actively in orienting the company's strategic direction. In short, the ownership structure of SOBs in Egypt, which are characterized by the ownership concentration and the domination of large institutional ownership, can act as an additional CG mechanism to control management activities and actions to ensure shareholders' interests.

6.2. Board Characteristics of Egyptian State-Owned Banks

The effectiveness of the BoD of banks and other corporations does not rely on the existence of the board, but rather on its size, composition, presidency, directors' nomination policy, the board performance and executive compensation policy. All of these board characteristics shall be analyzed with the exception of executives' compensation policies due to the lack of information on senior managers' compensation packages in banks' annual reports and other published documentations. The composition of boards of directors, precisely the proportion of NEDs is a measure of board effectiveness and independence. Boards which have a majority of NEDs are considered to be more independent and credible than others. In terms of the board duality; the board is considered to be more independent when its president is not the CEO of the bank. The following sections present a comprehensive analysis of the board size, composition and the dual direction of SOBs in Egypt.

6.2.1. Board Size

Regarding the size of the BoD in SOBs in Egypt, the law No.88 of 2003- that organize the activities of the Central Bank of Egypt, The Banking Sector and Money- indicates that the bank should be administered by a board of directors composed of nine members. As shown in figure 1, results revealed that BDC opted for the highest number of board members namely nine members and the other two banks (NBE and BM) have chosen a board of eight members. In sort, the average number of members per board is almost 9 members.



% of Banks included in the Study

Figure 1: Board Size in Eqyptian State-owned Banks

Board size is considered to be the crucial factor of the effective decision making. Vafeas (2005) suggested that there is no direct relationship between the board size and its performance. Both too small

and too large of the board size is likely to make it ineffective. (Jensen, 1993) argued that the ideal board size should not exceed eight or nine members and claimed that the board will be less effective when its size is more than eight members due to the coordination and process problems that contribute to weak monitoring. Although Bozec and Dia (2007) indicated that the board size for state-owned enterprises has a positive relation to technical efficiency, since bigger boards may be constructive for some companies as they provide diversity that would help companies to secure critical resources and reduce environmental uncertainties. However, other studies have indicated that small boards are more effective and linked with higher market values because the board members can communicate better among themselves, as well as easy to manage (Goodstein et. al. 1994).To conclude, the average number of members per board is almost 8 members in Egyptian state-owned banks, which are considered to be consistent with the effective average board size as per the previous studies (Jensen, 1993; Bozec and Dia, 2007). The average boards size in the studied banks make these boards more effective with regard to coordinating functions and monitoring management activities.

6.2.2. Board Independence

The board independence is measured by two variables; the proportion of NEDs versus EDs and the chief executive officer (CEO) duality (Weir et. al. 2002)). Boards with a significant proportion of NEDs can limit the practice of managerial discretion by exploiting their monitoring ability and protecting their reputations as effective and independent decision makers. Meanwhile, NEDs are required to provide independent assessment such as pay awards, executive director appointments and dismissals when dealing with the executive directors. An independent board of directors is believed to be a crucial mechanism for an effective control of management actions; these directors could be expected to be advocates of the shareholders' objectives (Fama and Jensen 1993a, 1993b). Boards dominated by NEDs may help to ease the agency problem by monitoring and controlling the opportunistic behavior of management since they (1) ensure that managers are not the sole evaluators of their own performance and (2) influence the quality of directors' decisions due to their independence, expertise, prestige and contacts and (3) they concern with maintaining their reputation in the external labor market (Jensen and Meckling, 1976; Pearce and Zahra, 1992; Fama and Jensen, 1993a,1993b). Figure 2 presents the results of the study about the independence of the boards of Egyptian state-owned banks in the following graph:

As shown in Figure 2, two thirds of BDC board of directors is NEDs and 50 % of board members in the other two banks (NBE and BM) are NEDs. In average, the percentage of NEDs on banks' boards of directors is 56%.

As indicated above, many studies argued that boards dominated by NEDs are more likely to act in the best interests of shareholders (Fama and Jensen, 1993a, 1993b; Brickley et. al. 1999). However, other studies found opposite results. They argued that NEDs are usually characterized by lack of information about the nature of business, do not bring the required skills to the job and, hence, prefer to play a less confrontational role rather than a more critical monitoring one (Franks et. al. 2001)). It is believed that the NEDs may not be able to exercise power, partly because they lack the superior information hold by EDs and partly because of time constraints as a result of multi-company independent outside director appointments. In addition, NEDs may lack professional knowledge about each business or the ability to monitor actions of the management. The EDs are better placed for evaluating company management. Moreover, the EDs benefit the company because of the extent of their firm specific information Raheja (2005).

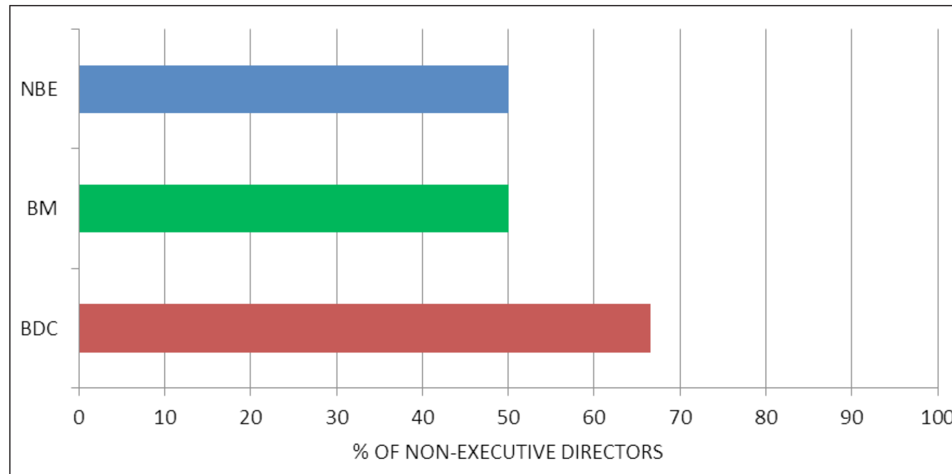


Figure 2: Board Independence in Eqyptian State-owned Banks (EDS - NEDS)

In SOBs in Egypt, the chairman of the board of directors and board members are selected by the Prime Minister in consultation with the Governor of the Central Bank for three years, based on their qualifications and experience in legal, economic, financial and monetary fields. All board members serve a maximum term of three years, and they are allowed to be re-nominated for other terms by the Prime Minister (the law No. 88 of 2003.

The second variable that measures the board independence and effectiveness is the board duality. The duality of direction refers to the person who has two powerful positions; the chairman of the board and the CEO, which would result in probability that this person hides unfavorable information to outsiders. Besides, it also enables the CEO to engage in opportunistic behavior since he/she has dominance over the board. When CEO duality exists, the CEO's decisions and actions may be directed to achieve his/or her own interests at the expense of the shareholders' interests. In Egypt, there are no mandatory rules for the separation of roles between both chairman and CEO. The adoption is recommended in the Egyptian Code of CG to separate the roles of chairman and CEO. The board is considered independent when its president is not the CEO of the company.

As per the shareholders model, (Jensen and Meckling (1976) suggests that CEO duality may limit board's ability to monitor management and therefore increase the agency cost. As a result, separating the CEO and the chairman of the board positions shall enhance firm performance. According to the banks' annual reports, the three state-owned banks have dual roles as the chairman of the board of directors is the CEO of the bank. The key contacts who have been interviewed argued that the CEO duality enhances the bank performance. Additionally, they emphasized that the separation between the CEO and the chairman of the board makes it difficult for the CEO to act in accordance with best interests of the shareholders. According to banks key contacts' perspectives, duality of direction can comprise certain advantages linked with the unification of leadership and a great knowledge of the bank's operating environment that should affect positively the bank performance. More specifically, duality of direction can help to (1) enhance the decision making process in banks by allowing a strong focus on banks' objectives and encouraging more smooth and fast implementation of operational decisions and (2) shape the destiny of banks with minimal board interference, which could also lead to improved performance resulting from clear, freed leadership of the board of directors. These perspectives are considered to be in consistent with Stewardship model (Brickley et. al. 1999).

The CEO is a corporation's chief strategist, responsible for initiating and implementing company-wide plans and policies. The Russell Reynolds Associates' Survey New York (2012) highlighted that board members are concerned with their independence from the CEO and are increasingly promoting that the chairman and CEO roles be separated to have a balance of power. While this trend is more established in Europe, data indicates that companies in the United States are imitating. While the trend toward separating the roles gains prominence, not all directors are in favor. According to survey, 41% percent of board members feel the chairman/CEO position should be one person. The effectiveness of BoD requires identifying lines of authority, responsibility and accountability for managers and be able to oversight their decisions (Basel Committee on Banking Supervision (2005).

6.2.3. The Board Roles and Responsibilities

As per the article 90 of Law No. 88 of 2003 on the Central Bank of Egypt, the Banking Sector and Money [62]: each state-owned bank shall have a board of directors to be formed as follows:

- Chairman of the BoD;
- Two deputy chairmen; and
- Six members specialized in banking, monetary, financial, economic and legal affairs with previous banking experience.

The chairman, the two deputy chairmen and directors shall be appointed by decree of the Prime Minister, after consulting the CBE's Governor, for a renewable three-year term. The salaries, allowances, and remuneration of the chairman and his/her two deputies, the remuneration of NEDs and the board attendance allowances shall be determined by decree of the Prime Minister.

Roles and Responsibilities of the Chairman: According to the law No. 88 of 2003 on the Central Bank of Egypt, the Banking Sector and Money, the chairman is basically responsible for enhancing the entire BoD performance and advising and directing the board. More specifically, the chairman roles and responsibilities are:

- To ensure that decisions are properly taken based on a full awareness of the subject matter and that decisions can be effectively and timely implemented and followed up;
- To encourage discussion and make sure that different opinions are expressed and discussed within the framework of the decision-making process;
- To ensure that the BoD acts effectively to serve the best interests of the bank and for avoidance of any potential conflict of interest;
- To maintain confidence among all directors in general and between EDs and NEDs in particular, enhance the relationship between the BoD as a whole and the senior management;
- To ensure the flow of adequate and accurate information on a timely basis to both directors and shareholders;
- To verify the effectiveness of the CG system applicable at the bank as well as the efficiency of BoD committees' performance;

- To ensure that all board members conduct a self-assessment which includes determining each member's compliance with the responsibilities of his/her job and the necessary requirements to boost efficiency; and

BoD: Duties and Responsibilities: In general, the BoD is fully responsible for supervising the bank management and in particular is responsible for the following:

- Approving and monitoring the execution of the bank strategies, policies and objectives;
- Approving risk policies and risk management policies;
- Approving, monitoring and upgrading the organizational structure and defining the bank structure of authorities and responsibilities;
- Selecting and replacing the bank senior executives after consultation with the CEO;
- Supervising and monitoring the senior managers' performance and ensuring that they are accountable to the BoD;
- Ensure that an effective information system that secures the efficiency of reports issued or received by the BoD is in place and timely provides all management levels in the organizational structure with key information timely;
- Holding periodic meetings with senior management and internal audit to review and discuss the policies and follow up the progress in accomplishing the bank strategic objectives;
- Monitoring and controlling any potential conflict of interests; and taking all necessary actions to overcome the relevant identified weaknesses;;
- Making necessary disclosures including disclosure to the CBE;
- Approving and reviewing the disclosure policies periodically and supervising policy implementation in line with the provisions of law and international standards;
- Evaluating, revising, approving and discussing with senior management regular and periodical assessments to ensure the efficiency and effectiveness of the CG practices and internal controls applicable at the bank;
- Disseminating the CG culture across the whole bank;
- Ensuring that an effective system that secures efficient reporting is in place;
- Allocating adequate time and efforts to ensure the sound performance of BoD's duties;
- Maintaining high and proper level of knowledge and experience among directors;
- Approving the strategies and policies related to risk management;
- Developing board members" skills and competencies and updating their knowledge;
- Setting mechanisms to compensate its staff according to their performance rates, as well as volume and level of their accomplishments pursuant to the Law No. 88 of 2003 on the CBE, Banking Sector and Money;

- Approving and periodically reviewing the bank policies related to the bases of IT management in general and information safety and security in particular.

The board duties and responsibilities are consistent with the OECD principles of CG and Basel Committee CG guidelines (OECD, 2004; Basel Committee on Banking Supervision, 2016).

6.2.4. Board Performance Evaluation

The purpose of the evaluation is to help the board achieve its objectives more efficiently and effectively. Boards should consider the issues that are appropriate to the bank's circumstances. These guidelines do not deal with individual director appraisal but banks are encouraged to move in that direction to comply with best international practices. In Egyptian state-owned banks, the evaluation of the board performance takes place on an annual basis. The evaluation process expands to include the board and its committees, both in terms of their internal performance by members collectively and how the committee performs from the perspective of the board. For instance, The BoD shall follow strict system for self-assessment to determine whether it and its committees are functioning effectively as a whole and as individuals. The individual assessment of each member is to identify the effectiveness of each member contributions to the BoD meetings and committees, and whether he/she has fulfilled his/her duties. The chairman is responsible for evaluating the members' performance by determining the strengths and weaknesses in the BoD, and if necessary making changes by reappointing and/or dismissing certain directors. In its annual report, the BoD shall disclose the performance evaluation process of the bank (Touny, 2014; Mubarak, 2011b).

6.3. Board Committee Structure

Concerning the role and the impact of committees, (Vafeas, 2005) found that there is an association between the existence of board committees and board effectiveness. The establishment of board committees is an effective means to transfer many activities of the board into specialized teams of directors that will focus on specific functions concerning a corporation's operations. Hence, a greater number of committees would result in greater involvement of the board members that would lead to greater effectiveness of the board (Sanchez, 2010). In the three banks under investigation, the roles and responsibilities of the board has documented in a board charter and associated policies. Banks' boards have established a number of committees, each is considered an integral part of the board and whose members are directors of the board. The fundamental role of these committees is to address topics in more detail, to manage conflicts of interest, to satisfy regulatory rules, and other relevant activities as necessary to ensure the proper CG of banks (Vafeas, 2005).

This study shows that each state-owned bank in Egypt has a board of directors, a permanent audit committee, and an executive committee. These norms are obligatory in the banks. Additionally, there are some other mechanisms that are not exclusive to banks, such as the board of directors, auditors, human resources committees, remuneration and compensation committees, governance and nomination committees and risk management committees. Other two committees exist in two banks out of the three, which are the investment policies committee and the information technology and banking technology committee. Furthermore, there is another mechanism that exists in one bank, which is the committee of informatics.

In the Egyptian banks, the board of directors is governed by the law No.88 of 2003 on the Central Bank, the Banking Sector and Money and the Law No.159 of 1981 on Commercial Companies. These

laws cover the composition, the board independence, the appointment of the chairman, deputy chairmen and members of the board, their rules and responsibilities and activities and the evaluation of the board performance. Moreover, these laws forced banks to create a permanent audit committee and an executive committee. In fact, effective supervision of banking institutions is essential to give their central role in payment transactions, credit and bankruptcy propagation from one bank to all other banks, even performing ones. Figure 3 shows the different obligatory and optional governance mechanisms used by Egyptian state-owned banks.

Duties and Responsibilities of Audit Committee: The role of the audit committee as per the three state-owned banks in Egypt (NBE; BM; BDC Annual Reports of 2015/16) is to:

- Nominate and determine the fees of the external auditors, and review issues related to their resignation or dismissal;
- Agree upon the scope of audit with external auditors;
- Review the annual financial statements before obtaining the approval of the BoD;
- Review annual financial statements prepared to be published and ensure their conformity with the financial statements data and the publishing rules issued by the CBE;
- Coordinate between the internal and external audit tasks and ensure the communications between the internal audit head and the external auditors on one side and the BoD and audit committee on the other;
- Review and approve the annual internal audit plan;
- Review the reports prepared by the internal audit department including reports on the adequacy and adherence to the bank's internal controls;
- Receive audit reports and ensure that the corrective actions were made by the competent departments on a timely basis with respect to the problems identified by the external auditors;
- Review the procedures adopted to enable the bank staff from reporting any possible violations with confidentiality;
- Submit a recommendation to the BoD to approve the annual compensation for the internal audit function as a whole including bonus for performance appraisal;
- Evaluate the internal audit function;
- Approve or submit a recommendation to the BoD to approve appointing, re appointing or dismissing the internal audit head and chief internal auditors;
- Provide the CBE quarterly with a copy of the report issued after the committee's meeting, as stipulated in article 82 of Law No.88/2003 and article 28 of its Executive Regulations including key remarks, procedures taken or any other significant issues.

The independence of audit committee is based on proportion of NEDs on the committee. As per the Law No. 88 of 2003 and the law No. 159 of 1981, the audit committee in banks must be dominated by NEDs, where the committee is composed of three NEDs with an appropriate mix of competencies, experience, and sufficient knowledge in financial, auditing and accounting fields. This independence of the audit committee

shall increase the effectiveness and efficiency of the board in monitoring the financial reporting process of a bank. According to the shareholders model, the independent members in audit committee can help the principals to monitor the agents' activities and reduce benefits from denying information. This is the case in Egyptian state-owned banks, whose audit committees are dominated by NEDs.

As per the laws and regulations, all state-owned banks in Egypt shall have executive committees. According to the law No. 88 of 2003 on the CBE, the Banking Sector and Money, the executive committee is properly constituted of the executive directors and the bank's CFO and presided by the bank chairman. The committee may seek the assistance of any officers or employees it deems appropriate from the Bank staff. The duties and responsibilities of the committee are [The Law No. 88 of 2003; The Law No. 159 of 1981[63]:

- Setting the bank's objectives and corporate strategy;
- Consider and take decisions related to finance and credit facilities within the scope of its delegated authorities;
- Consider and take decisions on equity participations within the scope of its delegated authorities;
- Discuss on reports classifying finance/credit facilities provided by the bank to its customers and the corresponding proposed provisions, and reports on equity participation assessment to be submitted to the BoD with its recommendations;
- Discuss and recommend the required amendments on the bank's organizational and functional structure and workflow regulations;
- Undertake other functions decided by the bank rules and regulations;
- Following up the execution of the bank's strategy and ensuring that the strategy is implemented as per the approved action plan;
- Following the execution of the bank's budget and making required corrective actions;
- Studying and approving new products offered by the bank.

While, the credit committee is one of the committees that is established by the BoD and whose major responsibility is to review the quality of the bank's credit and investment portfolio; supervising the effectiveness and administration of credit-related policies; and approving loans and investment above management limits (NBE; BM; BDC of 2015/16) .

All SOBs in Egypt have HR committees. This committee includes board members and some representatives for top management, including HR Head or his/her substitute. The committee may invite employees or persons from inside or outside the bank to help in performing its activities. The main duties and responsibilities of this committee are (NBE; BM; BDC of 2015/16):

- Revise and approve HR policies;
- Present and propose HR strategies in consistent with the bank's strategy and objectives;
- Develop proposals regarding salaries structure;
- Approve all compensation and benefits policies and regulations;
- Discuss and present any other issues that need to be approved by the BoD.

The three state-owned banks in Egypt have remuneration and compensation committees (namely in some banks a compensation and benefits committee) and governance and nomination committees (namely in some banks a corporate governance committee). The later committee focuses on ensuring that directors' appointments and compensations are based on merit rather than on social network. An effective nomination committee should therefore ensure that NEDs interests are aligned with those of the shareholders and so help decrease agency costs. More specifically, governance and remuneration committees must ensure that strategic human resources' selection, performance pay schemes, policies are aligned with banks strategies and policies. The governance and nomination committee consists of 3 NEDs. Furthermore, it is responsible for ensuring firm compliance with the principles of CG and all relevant laws and regulations imposed by the CBE and all other regulatory bodies (NBE; BM; BDC of 2015/16).

While the former committee (remuneration and compensation committee) must ensure that promotion, remuneration, retirement and dismissal of senior management are made on merit and performance evaluation, and high level succession planning is made properly. This committee consists of 3 NEDs ((NBE; BM; BDC of 2015/16)). Additionally, all state-owned banks in Egypt have risk management committees, which review and approve the bank's key risk policies on the establishment of risk limits relating to operational and information security risks and receiving reports on the compliance with significant limits. This committee is responsible for reviewing the bank's regulatory risk capital (credit, market, liquidity and operational risks), including significant inputs and assumptions.

Furthermore, two SOBs in Egypt have investment policies committees and IT & banking technology committees. The former committee is responsible for evaluating and allocating the investment budget on the bank's macro level. While, the later committee is responsible for proposing and executing IT and banking technology plans ((NBE; BM; BDC of 2015/16).

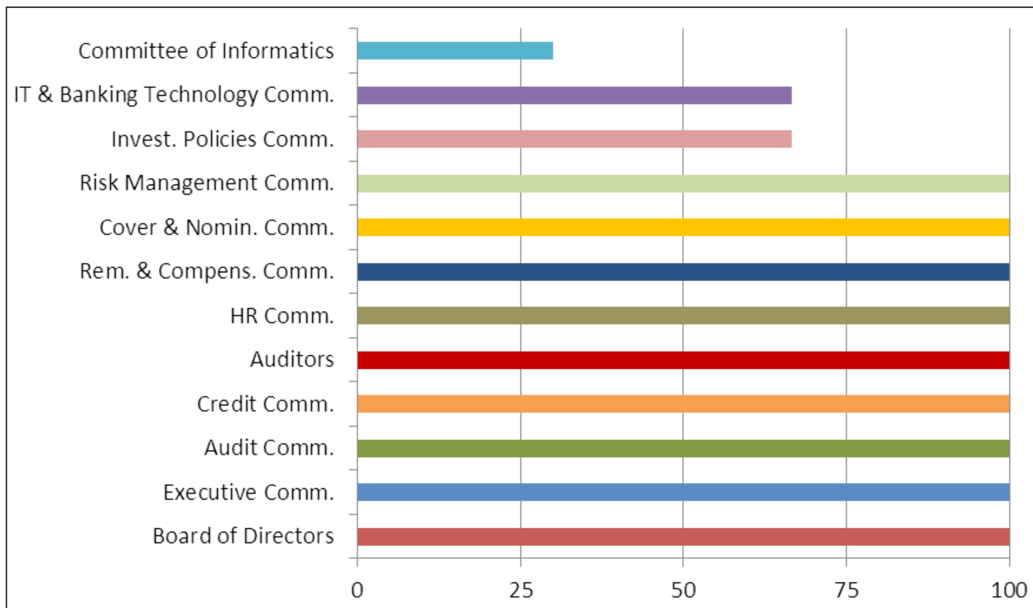


Figure 3: Corporate Governance Mechanisms Adopted by Egyptian State-Owned Banks

Finally, BM has a Committee of Informatics, which monitors the offered services and ensures that these services are in consistent with the highest standards, to maximize the return on the bank's investments in

the field of informatics (BM, 2015/16). The forgoing analysis of the board activities, including the existence of board committees and their roles, composition and responsibilities indicate that all SOBs in Egypt have committees forced by the laws and regulations, such as audit committees and executive committees. Furthermore, all banks under investigation have other committees created voluntarily to strengthen CG systems in these banks such as HR, risk management, governance and nomination, remuneration and compensation committees. The board committees in the three banks are increasingly independent due to the domination of NEDs on these committees.

6.4. The Role of External CG Mechanisms in the Banking Sector

The deep analyses of Egyptian state-owned banks' annual reports show that most of these banks have no information about external CG mechanisms. Nevertheless, it does not mean the absence of any role of these mechanisms in the CG of the banks. This finding emphasizes the importance of internal CG mechanisms vis-à-vis the external ones in the banking sector (Damak, 2013). The discipline exercised by external CG mechanisms is ineffective because of the high opaqueness. It affects relationships between managers and board of directors in the bank. Similarly, it can affect the relationship between shareholders and other partners of the bank, including creditors, depositors and regulators. Other characteristics of the banking sector may explain the dominance of internal CG mechanisms in banks, for example competition in the services market is low at banks, given that managers establish barriers to access to information needed by developing a net of relationships with their customers (Levine [67]). Competition among banks is limited by the shareholding of the state that holds the full equity of these banks, which also prevents the entry of new competitors. Thus, foreign investors would be less willing to compete with local banks. The efficiency of the stock market is also weakened by the presence of the regulations and the high gratitude of banks (Levine, 2014).

7. CONCLUSIONS AND FUTURE RESEARCH

CG is linked with the evolution of modern business and the separation between ownership and control. CG does not only concern the shareholders and managers. But, it expands to include all the relationships that managers have with stakeholders, including employees, suppliers, customers, creditors, depositors and shareholders. It was necessary to start the paper by presenting the theoretical backgrounds of the CG; since there is a huge need to understand the ability to provide the remedy. The need is driven from the conflict of interests between managers and stakeholders, especially shareholders. These conflicts lead to unfavorable implications for the firm. The appropriate remedy could be a system of CG comprising internal CG mechanisms such as the board of directors, the audit committee, the auditor, the credit committee the executive committee and external mechanisms that are mainly the financial market, the market of goods and services and the labor market of managers. However, the presence of one or more of these governance mechanisms is not in itself a guarantee of efficiency. Hence, the effectiveness of the board of directors and the board committees depends on its size, composition (NEDs and EDs), presidency, roles, authorities and responsibilities.

This exploratory study indicates that most of CG mechanisms adopted by Egyptian state-owned banks have been forced by the laws and regulations, all banks under investigation have a board of directors, an auditor, an audit committee, credit committee and an executive committee. However, many banks

have formed committees voluntarily to enhance CG structures, such as HR, nomination and governance, remuneration and compensation, and risk management committees. Several CG mechanisms used by the three state-owned banks in Egypt are increasingly adopting a more independent board of directors. These governance mechanisms include the board scope of power, the board full responsibility for CG, the board appointment by decree of Prime Minister after consulting with governor of the Central Bank of Egypt, and the board size and composition at SOBs. Furthermore, the dominance of NEDs on board committees is enhancing the adoption of board independence and the effectiveness of CG. However, the paper concludes that there is duality of direction between the chairman of the board and the CEO of the bank, which is attributed to advantages linked with the unification of leadership and a great knowledge of the bank's operating environment that should affect positively the bank performance. The paper reflects the significant improvements that have been made by Egyptian state-owned banks regarding corporate governance, but more efforts remains to be done, such as the full transparency of banks' activities and complete accountability. In addition to, the need of Egyptian banks to opting for specific performance measures and standards for evaluating the board performance. Finally, it indicates the importance of internal CG mechanisms vis-à-vis external norms.

This paper suggests new avenues of future research for institutional perspectives of CG, such as the degree to which these banks adhere to external CG mechanisms; the relationship between CG mechanisms and the bank performance, CG mechanisms opted for by private and joint venture banks. Additionally, one of the CG themes that need more exploration and investigation is CG in other state-owned enterprise; particularly the empirical research in this area is so limited. The study provides theoretical implications, where it helps to fill the theoretical gaps in literature review in terms of CG in developing countries in general and CG in the banking sector in particular. Also, the paper provides practical implications, including insights and ideas for policy makers and stakeholders to maintain effective corporate governance systems to improve the effectiveness of financial institutions.

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