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Corporate Governance in Gulf Cooperation Council (GCC) Countries: Ownership Structure, Executive Compensation and Firm Performance

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List of Abbreviations

BFH	Bahrain Financial Harbour
CEO	Chief Executive Officer
CMA	Capital Market Authority
DIFC	Dubai International Financial Center
e.g.	exempli gratia
EU	European Union
FDI	Foreign Direct Investment
FTA	Free Trade Area
FTSE	Financial Times Stock Exchange
GCC	Gulf Cooperation Council
GDP	Gross Domestic Product
HI	Herfindahl Index
i.e.	id est
IMF	International Monetary Fund
MENA	Middle East and North African
NRC	Nomination and Remuneration Committee
OECD	Organisation for Economic Co-operation and Development
OLS	Ordinary Least Squares
REITs	Real Estate Investment trusts
ROA	Return on Assets
ROSC	Report on the Observance of Standards and Codes
SAMA	Saudi Arabian Monetary Agency
SWFs	Sovereign Wealth Funds
TCT	Transaction Cost Theory
UAE	United Arab Emirates
UK	United Kingdom
US	United States
USD	United States Dollar

Abstract

Gulf Cooperation Council (GCC) countries showed a remarkable economic growth in the past decade due to being a major oil exporter, attracting significant foreign investment, becoming a major global trading partner and integrating further to the global economy. These developments have resulted in the need to institute advanced corporate governance norms for GCC companies. However, corporate governance systems and practices in the GCC countries are of recent origin and, albeit the importance of corporate governance practices in transforming GCC economies, there is a dearth of academic research on corporate governance in GCC countries. Our motivation for this research is the increasing importance of GCC economies within the world economy and the lack of research on corporate governance mechanisms in these countries. We believe we make a significant contribution to the existing research by providing comprehensive empirical insights into different aspects of corporate governance practices and firm performance in the GCC countries. In particular, our focus is on how corporate performance is affected by ownership structure and executive compensation. We test these relationships using a uniquely constructed and hand collected data of 349 listed companies in Kuwait, Saudi Arabia, Oman, Qatar and United Arab Emirates for the years between 2006 and 2011.

We start by formulating a theoretical base for the study through a discussion on how major theories of corporate governance evolved over time and reviewing the state of empirical research in corporate governance in general as well as in the context of the GCC region. We find that the corporate governance practices and standards prevailing in the GCC countries are not comparable to those followed in other developed countries because of many challenges identified by previous research. We also find that there is a large scope for the implementation of globally comparable corporate governance practices in the GCC countries.

In our first empirical analysis, we investigate the impact of ownership structure on firm performance. The issue as to whether ownership structure matters for the performance of firms has been an important subject of debate in the corporate finance literature. Our objective here is to explore in more detail the factors that motivate particular types of ownership structure and the potential impact of ownership structure and firm performance in the Gulf region. We find that higher insider ownership leads to better performance,

especially when insider owner is the Chairman. A larger ownership by institutional investors has a positive impact on firm performance. On the other hand, we find that GCC firms with high family ownership perform does not perform well.

In our second empirical analysis, we examine the key determinants of the executive compensation to top five executives in GCC firms. We find that larger firms and firms with potential future growth pay higher total compensation to their executives. Concentrated ownership structure leads to lower compensation levels while firms with high family ownership as well as external ownership tend to pay higher compensation. We also find that managerial as well as institutional ownership of companies tends to lead to higher salaries. Companies that have more growth potential seem to pay higher bonuses. We also find that the choice between behaviour versus outcome oriented compensation is mainly influenced by firm size, the presence of executive members on the board, and managerial ownership. Larger companies prefer to pay bonus as part of executive compensation. Companies that have higher number of executives or owned by managers are also tend to pay more compensation through bonuses.

In our third empirical analysis, we examine the relationship between executive compensation and firm performance. We find that higher total executive compensation leads to better firm performance. On the other hand, we do not find any significant relationship between the components of compensation (salary and bonus) and performance. We point out that specific GCC economic environment and features peculiar to this region has more impact on the firm performance rather than the executive compensation.

Overall, findings of our study is valuable in assisting key decision-makers, such as the shareholders or policy makers, in enhancing firm performance through diversifying their ownership structures and utilising the right policies in compensation of executives in GCC countries.

Chapter 1. Introduction

Gulf Cooperation Council (GCC) countries[1] showed a remarkable economic growth in the past decade. The size of GCC economy tripled between 2002 and 2008 rising to USD 1.1 trillion. Although there was a decrease in the growth of the region in 2009 because of the repercussions of global financial crisis, it rebounded in 2010 and 2011 growing by 17.6% and 9.5% respectively. Further growth in the GCC economy is seen during the 2011-2014 period (GulfBase, 2014). Several factors lead this economic performance. Firstly, being in possession of around 40% of the global oil reserves, GCC countries are major exporters of oil and have occupied a prominent position in the supply of petro-carbon products to many countries in the world. Secondly, global demand for oil has led GCC countries to experience a significant increase in their trade volume and this has necessitated the integration of the corporate and financial systems of these countries with those of other global economies calling for effective corporate governance in the region. Thirdly, several domestic and transnational countries have made significant investments in the business of oil exploration and refining as well as on the development of new oil fields making the GCC region a major regional trade hub paving way for the integration of the region with the global economy (Sturm et al., 2008). Fourthly, various free trade agreements that GCC countries entered into with other major economies, such as the European Union, have contributed to the integration of GCC economies to the world economy and to assume a position of a major international trading partner with many countries. Finally, the GCC economies are keen to diversify their economic activities to many other industries rather than depending mainly on oil sector. While this industrial diversification takes place, it is important to ensure that the balance between economic and social goals is maintained by implementing suitable corporate governance norms within the GCC region (Weir, 2011). Overall, these developments and changes in GCC economies have resulted in the need to institute stricter corporate governance norms for

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[1] Arabian Peninsula or Gulf consists of Saudi Arabia, Kuwait, Bahrain, Qatar, the United Arab Emirates and Oman. These six countries founded the Gulf Cooperation Council (GCC) in Abu Dhabi, United Arab Emirates, in May 1981. The objective of the association is to promote social and economic integration among the member countries in all fields. The GCC countries have been implementing a number of policies for supporting the economic diversification and develop of infrastructure in their respective countries. GCC region has progressed to be a Free Trade Area (FTA) in 1983. The customs union agreement entered into in 2003 focused on removing the restrictions on internal trade and establishing customs tariff common to all member countries. The GCC also floated a common market status agreement in 2008 providing for a single market environment in which the citizens of all member countries could enjoy equal rights and privileges. However, the customs union agreement passed in 2003 has not fully taken effect yet (Al-Momani, 2008).

GCC based corporations which in turn can perform effectively in the international marketing arena. We explain the implications of these developments on corporate governance issues in the GCC counties below.

Having assumed a prominent role in the global trade and markets requires a closer cooperation with both developed and developing economies around the world both at political and economic level (Ulrichsen, 2011). However, the cultural and religious aspects in the GCC economies have remained largely local with no intention of these economies to adopt broader international perspectives in their dealing with other nations (Ulrichsen, 2011). It may be possible for the GCC countries to strengthen the economic ties and relationships with other economies by developing and instituting strong corporate governance measures. However, corporate governance has a strong relationship with local business environment and practices and the ownership patterns prevalent domestically and it is argued that these aspects (such as business practices and ownership patterns) are substantially different in GCC region when in comparison to advanced economies. Such differences may make it difficult for the GCC nations to accomplish the desired levels of integration with global businesses (Weir, 2011).

Despite making rapid progress in economic development, corporate governance practices of GCC firms could not keep up with the speed of adjustment and corporate governance are still in the nascent stage (Musa, 2002; Al-Zuhair 2008). It is suggested that this lack of corporate governance can lead to lacklustre performance by corporate entities (Gellis et al., 2002; Islam and Hussain, 2003). Many factors have contributed to the slow progress in the operation of effective corporate governance mechanisms in the GCC region. These economies are characterised by the presence of extensive family control, under-developed capital markets and lack of need for external capital which can be considered as reasons for slow progress in establishing an effective structure of corporate governance (Al-Zuhair 2008). These characteristics distinguish GCC economies different from other Anglo-Saxon and Western economies in the matter of ensuring effective corporate governance.

Out of these, literature has identified ownership structure as one of the main reasons for the ineffective corporate governance in the region (e.g. Saidi, 2004; Al-Zuhair, 2008; Weir, 2011; Musa, 2002). Control of the corporate entities by few shareholders and the

presence of family ownership have been found to hinder the development and adherence to stricter corporate governance norms and practices. Some of the major corporations are government owned; this also poses a challenge in managing the corporation by following effective governance norms. Unlike developed countries, lack of separation of ownership and management is often observed in the GCC corporations. Such separation is critical for ensuring stricter corporate governance practices. It is also observed that there is only limited number of independent directors in the boards and more often the functions of both CEO and Chairman are carried out by the same person that would act against following governance practices effectively. Unlike in the developed countries, the high concentration of ownership diminishes the effect of following effective corporate governance practices in the GCC region (Yasin and Shehab, 2004; World Bank, 2003; FRC, 2012).

High level of family ownership is another reason for the ineffective corporate governance in the region. Family-owned companies in GCC countries have weak corporate governance practices and mostly they are reluctant to change the old ways of doing their business transactions (Saidi, 2004). The resistance from the family-owned firms may be due to the impact of factors like fear of losing the control over the business by the family, fear of losing competitive advantages of business due to increased transparency and additional disclosures, fear of lack of knowledge of the new corporate governance practices and failure to recognise the advantages that might arise from the use of better corporate governance practices with respect to succession planning, accessing external sources for infusion of additional capital and better firm performance.

The closed control structure of companies in GCC region has eliminated the presence of external shareholders and led to lower levels of external ownership. This has given absolute control of companies in the hands of few families and in some cases to the government undermining the need for the institution of corporate governance norms comparable to international standards (Union of Arab Banks, 2003). Another factor that hinders the development of effective corporate governance mechanism in the region is the absence of a well-developed capital markets in the GCC economies. Rizvi and Masih (2014) point out that there still exist certain limitations such as regulatory weaknesses, relatively smaller number of firms having large institutional holdings and excessive dependence of listed firms on oil dependent sectors which characterise the capital market

in the GCC region and account for the ineffectiveness of such markets as compared to the markets in developed countries. They also highlight that the regulatory structures have not been developed to meet the international standards as the capital markets in the region continued to remain small and ineffective. Reason for underdevelopment of the capital markets may be traced to the fact that the businesses in GCC region are more dependent on internal capital sources or the governments for funding avoiding the necessity to invite external capital. Even for expansion and growth, the major corporations do not expect any external sources to fund the capital requirements. Hence, the corporate governance structures in GCC countries have not developed in tandem with its development in developed economies.

Thus, corporate governance systems and practices in the GCC countries are of recent origin resulting in some deficiencies in the implementation of the practices. Although the corporate governance standards and regulations in many of the GCC countries are generally in line with established international standards, the regulators in the respective countries are not keen in implementing the standards effectively. One of the impediments for slow progress in this respect is the absence of any stringent punishments for the failure on the part of corporations to adhere to the set norms. Lack of interest of the officials and authorities in the implementation of stricter corporate governance norms and practices has led to a high level of subjectivity affecting the seriousness of the regulations introduced to ensure better governance (Al-Zuhair, 2008; Weir, 2011). According to Weir (2011), the effectiveness of corporate governance and transparency in the dealings of corporations in the GCC region has been found to be low as compared to other developing countries. They point out that excessive control over media and lack of freedom of press restricts the chances for the shareholders and other investors to obtain factual information on the internal affairs of corporations. Moreover, the absence of investor activism and excessive government control over corporations have hindered the progress in instituting effective corporate governance measures in countries like Kuwait and Saudi Arabia in the GCC region.

Empirical as well as theoretical research on corporate governance of GCC countries is rather limited. This is because the corporate governance mechanisms that could work in GCC countries differ drastically from those being practiced in the Western and other advanced countries. Available literature points out to a situation where the level of

disclosure by the corporations in GCC countries is generally below par and the corporations do not wish to part with information that would benefit the investors and general public in their investment decisions and the corporations are rather unwilling to provide information that are deemed critical in other jurisdictions (Union of Arab Bank, 2003). These findings provide evidence to show that the existing corporate governance standards in GCC countries are not comparable to international standards which also signifies the fact that there exists a considerable scope for improving the effectiveness of corporate governance practices in the region (Al-Zuhair, 2008; Weir, 2011).

Sourial (2004) has given a different and important dimension to the research on corporate governance practices in GCC region. He points out that most of the corporate governance standards meant to be followed in the region are drawn from Anglo-Saxon models. The main issue with these standards is that such standards are misfit to the existing cultural and societal values of owners and firms in the GCC region resulting in major problems of implementation of the standards. This finding leads to the situation that GCC economies should strive to develop their own corporate governance norms and practices based on Shariah law rather than copying the practices from Anglo-Saxon models.

It is reported that the development of corporate governance standards in the GCC region has not been satisfactory (Al-Zuhair, 2008). However, certain states have shown the ability to put in place stricter corporate governance norms as observed in the cases of Dubai International Financial Center (DIFC) and Bahrain Financial Harbour (BFH) which have stronger norms for the firms operating from within these areas. Also, for example, UAE is generally shown as a country with better corporate governance practices within the region[2]. Al-Zuhair (2008) is of the opinion that there is no actual need for developing internationally comparable corporate governance norms by the authorities in

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[2] Bhatti et al (2006) found UAE within the GCC to have developed reasonably stronger structure of corporate governance because of the formation of free trade zones and the presence of international businesses within such zones. Since each zone has an independent regulator having the powers to make policies and to adjudicate, it has been possible to make tougher and stricter corporate governance procedures and practices as compared to those of other GCC economies compelling international institutional investors to confine themselves to the free trade zones. Adawi and Rwegasira (2011) observe that while UAE is able to offer a unique corporate governance environment, the present system of mandatory requirements under corporate governance regulations are still found to be short in meeting the international standards. The study finds that existence of a quality corporate board may be vital to ensure the adherence to the desired level of voluntary adoption of corporate governance measures. Presence of more number of independent directors with diversified backgrounds and experience in the corporate boards may serve to meet the purpose of achieving effective corporate governance in the GCC region (Baydoun et al. 2013).

the GCC countries which led to slow progress in this direction. However, Rehman (2010) observes that there is an increasing trend of foreign institutional investors wanting to enter GCC counties for their investments. Therefore, there is the need for these countries to develop and implement stronger corporate governance practices to attract more such institutional investors. Thus, previous research has shown that although the corporate governance scenario may vary from one jurisdiction to another within the GCC region, there is strong need and sufficient scope for further development in the matter of implementing stricter corporate governance norms.

Albeit the importance of corporate governance practices in transforming GCC economies, given the abovementioned factors, there is a dearth of literature on corporate governance in GCC countries. Therefore, our main motivation here is the increasing importance of GCC economies within the world economy and the lack of research on corporate governance mechanisms of GCC countries' corporations.

We make a significant contribution to the existing research by providing comprehensive empirical insights into different aspects of corporate governance practices and firm performance in the GCC countries. In particular, our focus is on how corporate performance is affected by ownership structure and executive compensation. We test these relationships using a uniquely constructed and hand collected data of 349 listed companies in Kuwait, Saudi Arabia, Oman, Qatar and United Arab Emirates for the years between 2006 and 2011.

This research contributes to the existing literature in several ways. Firstly, to our knowledge, this is the first study to focus on the impact of different types of ownership structures on firm performance in the GCC countries. In particular, we assess the influence of different types of ownership structures (such as managerial ownership, family ownership, government ownership, institution ownership, foreign ownership and concentrated ownership) on firm performance. Earlier studies have focused on a single factor or other sectors [Family ownership on bank performance (Arouri et al. 2014); government ownership (Zeitun and Al-Kawari, 2012)]. These studies are not comprehensive to cover the impact of different ownership structures on firm performance. In order to emphasise the relative advantages of using a particular ownership structure,

this study has taken into consideration a variety of ownership structures that are investigated mainly for developed countries but not for the GCC region.

Secondly, in this research we investigate the determinants of executive compensation in the GCC countries. To this extent, we are not aware of any other research looking at how firms in the GCC remunerate their managers. In this context our study is unique due to the limited number of earlier studies conducted in GCC countries (e.g. Joshi and Wakil, 2004; Baydoun et al. 2013; Al-Saidi and Al-Shammari, 2013; Abraham, 2013). These studies are not comprehensive enough mainly because of the lack of sources and opportunities available to collect data on reasonably large size of samples in the GCC region resulting from poor reporting by companies. In our work, we focus on how total compensation and its components as behaviour oriented (salary) and outcome oriented (bonus) compensation are shaped by firm characteristics, ownership structure, and other corporate governance mechanisms.

Thirdly, the impact of executive compensation on firm performance is rarely studied in the context of GCC countries. Exceptions are Aljifri and Moustafa (2007) suggesting the introduction of suitable corporate governance mechanisms to improve firm performance, Hassan and Halbouni (2013) recommending the adoption of accounting-based performance measures and Al-Swidi et al (2012) pointing out the cultural impact on firm performance. The earlier studies did not cover the specific impact of different components executive compensation on firm performance in GCC region using large set of panel data and report on there on. Our study on executive compensation and firm performance in GCC countries has bridged this research gap by considering multiple components of executive compensation using large panel data in the GCC context and their impact on firm performance in the region.

Finally, our contribution to the literature is related to the size and the coverage of the data. We employ a large cross country sample that covers 349 firms from the GCC region. The data is gathered from different sources, namely, Thomson one banker, Thomson.com, Datastream and annual reports. In particular, all of the board characteristics and compensation structure data are manually collected from the annual reports. Given that our data is in panel data design, we employ panel data regression techniques to estimate our empirical models to examine the relationships between the explanatory and response

variables. In particular we use a combination of fixed effect, random effects and pooled-OLS regressions in our empirical chapters.

Panel data analysis is suitable to the task in hand because it is a regression approach that combines both time-series and cross-sectional data (Baltagi, 2005). Panel data enables a researcher to include variables that cannot be measured or observed such a differences in business practices across companies or differences in culture across countries. It also enables a researcher to analysis variables that change with time but not across firms. In general, panel data analysis controls for individual heterogeneity and often analysed using two techniques including fixed effects and random effects models (Baltagi, 2005; Torres-Reyna, 2007).

This thesis has four main sections. Chapter 2 presents a detailed background review of theoretical perspective of corporate governance and empirical studies focusing on the GCC region. Chapter 3, Chapter 4 and Chapter 5 are empirical chapters examining the links between ownership structure, executive compensation and firm performance. Below we explain these sections in detail.

Chapter 2 provides a background for this study. It reviews the literature on major theories, corporate governance approaches, an overview of corporate governance on emerging markets and historical perspective of corporate governance in Gulf Countries. This chapter of the research have identifies that the scope of corporate governance can be defined through agency theory and stakeholder theory and the two popular approaches to corporate governance are Anglo-Saxon approach and the multi-stakeholder approach.

Chapter 2 contributes to this research by presenting a critical understanding of the state of research in corporate governance in general and in the GCC region in particular. The chapter is divided into several sections. The first section focuses on the various theories of corporate governance that have evolved over the years. The second section reviews the different approaches to corporate governance. The third section identifies the pattern of development and state of corporate governance in the developing and emerging markets. The fourth section is concerned with the critical analysis of the development of corporate governance in the Gulf region of Middle East and the final section is concerned with

critical examination of the issues in corporate governance as it is practiced in GCC countries.

In Chapter 3 we investigate the impact of ownership structure on firm performance. The relationship between ownership structure and firm performance is important in shaping the corporate governance framework of a firm (Jensen and Meckling, 1976). The issue as to whether ownership structure matters for the performance of firms has been an important subject of debate in the corporate finance literature. The empirical evidence on the impact of ownership structure on firm performance is mixed and sometimes contradictory. Some studies find that there is no significant relationship between ownership structure and firm performance (see for example, Loderer and Martin, 1997; Agrawal and Knoeber; 1996 and Firth et al. 2002).

However, a large number of studies have shown that ownership structure affects performance. It is argued that ownership structures that affect performance negatively are ownership concentration (Johnson et al., 2000; Gugler and Weigand, 2003; Grosfeld, 2006; Holmstrom and Tirole, 1993), government ownership (Xu and Wang, 1999; Sun and Tong, 2003), family ownership (DeAngelo and DeAngelo, 2000; Fan and Wong, 2002; Schulze et al., 2001; Demsetz, 1983; Fama and Jensen, 1983; Shleifer and Vishny, 1997) and managerial ownership (Demsetz and Lehn, 1985). On the other hand, structures with positive impact on the firm performance are foreign ownership (Arnold and Javorcik, 2005; Petkova, 2008; Girma, 2005; Girma and Georg, 2006; Girma et al., 2007; Chari et al., 2011; Mattes, 2008), managerial ownership (Jensen and Meckling, 1976; Chen et al., 2005; Drobetz et al., 2005)[3], institutional ownership (McConnell and Servaes, 1990; Han and Suk, 1998; Tsai and Gu, 2007), family ownership (Anderson and Reeb, 2003; Villanonga and Amit, 2006); Maury, 2006; Barontini and Caprio, 2006; Pindado et al., 2008) and government ownership (Sun et al., 2006).

Several global economic developments make the empirical work in Chapter 3 worthwhile to undertake. Firstly, as mentioned above, GCC countries remain as major global economic players as oil producers. Secondly, despite its future economic prospects, it is argued that the GCC countries suffer from corporate governance issues (Musa, 2002). The development of corporate governance in the region and the governing rules has

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[3] Furthermore, some studies suggest that there is no link between insider ownership and performance (e.g., Davies et al., 2005; Himmelberg et al., 1999).

largely been influenced by religion, i.e. Islamic Sharia law (Gellis et al., 2002), which reflects the cultural and religious characteristic of the region (Islam and Hussain, 2003). Previous studies have argued that most businesses are controlled by a few shareholders and family ownership as well as state ownership is prevalent in the management of companies (Saidi, 2004; Union of Arab Banks, 2003). In addition, corporate boards are dominated by controlling shareholders, their relatives and friends and there is no separation of ownership which is often observed in developed countries. The number of independent directors in the boards is limited and the functions of the CEO and Chairman are carried out by the same person. The high concentration in firm ownership therefore undermines the principles of good corporate governance that are prevalent in western settings (Yasin and Shehab, 2004; World Bank, 2003; FRC, 2012). Thirdly, there is a dearth of literature on the impact of ownership structure on firm performance in GCC countries. Rare examples are Arouri et al. (2014), who find that bank performance is affected by family ownership, foreign ownership and institutional ownership and that there is no significant impact of government ownership on bank performance and Zeitun and Al-Kawari (2012) who observe a positive impact of government ownership on firm performance. Undertaking the work in Chapter 3, we are motivated by the mixed results obtained in previous studies and the limited number of studies that have focused on GCC countries. The objective of Chapter 3 is to explore in more detail the factors that motivate particular types of ownership structure and the potential impact of ownership structure and firm performance in the Gulf region.

Our findings in Chapter 3 show that higher insider ownership leads to better performance, or a higher Tobin's Q, especially when insider owner is the Chairman. A larger ownership by institutional investors has a positive impact on firm performance. On the other hand, we find that GCC firms with high family ownership perform worse. We also find that government ownership is negatively associated with performance when ROA is used as the performance measure.

In Chapter 4, we empirically explore the key determinants of the executive compensation. Previously, a large number of empirical studies has focused on the determinants of executive compensation in different research contexts and settings (see for example, Fung et al., 2001; Schipani and Liu, 2002; Core et al., 1999; Vafeas, 2003; Carothers, 2004). However, there are limited number of studies (e.g. Joshi and Wakil, 2004; Baydoun et al.

2013; Al-Saidi and Al-Shammari, 2013; Abraham, 2013) that have focused on GCC countries on the determinants of executive compensation.

In Chapter 4, we are motivated by the mixed results obtained in previous studies and limited research in this area on GCC countries. The objective of Chapter 4 is to explore the determinants of the executive compensation in the GCC countries. The study distinguishes between bonus and salaries paid to top five executives and it also examines the choice of compensation method (salary or bonus) by GCC firms. The question as to whether market-based corporate governance mechanisms on executive compensation that are successful in developed countries would be effective in emerging economies remains debatable, especially in the light of nascent nature of corporate governance mechanisms prevalent in GCC countries. This makes the subject matter of this study more interesting and appropriate. In particular, the focus of the research was to explore how total compensation and its components as behaviour (i.e. salary) and outcome (i.e. bonus) oriented are shaped by firm characteristics, ownership structure, and other corporate governance mechanisms. Additionally, the research also examined the determinants of the choice of compensation type (namely behaviour versus outcome) by the GCC firms. We use publicly available data (from company annual reports) on total compensation paid to the executives.

Our results in Chapter 4 reveal that in the GCC countries larger firms and firms with potential future growth pay higher total compensation to their executives. Concentrated ownership structure leads to lower compensation levels while firms with high family ownership tend to pay higher compensation. There is also evidence that external ownership leads to higher total compensation. In terms of behaviour-oriented compensation (i.e. salary), we find that larger firms and firms with higher leverage pay higher salaries to executives. Firms that have a chairman from the family and have higher presence of executive members in the board tend to pay lower salaries. The findings of Chapter 4 indicate that managerial as well as institutional ownership of companies tends to lead to higher salaries. In terms of outcome-oriented compensation (i.e. bonus), the study finds evidence that companies that have more growth potential pay higher bonuses. A family related chairman and higher number of executive members in the board is related positively to bonus payments. There is also evidence that ownership by managers and by family results in higher levels of outcome-oriented compensation. We also find

that the choice between behaviour versus outcome oriented compensation is mainly influenced by firm size, the presence of executive members on the board, and managerial ownership. Larger companies prefer to pay bonus as part of executive compensation. Companies that have higher number of executives or owned by managers are also tend to pay more compensation through bonuses.

Subsequently, Chapter 5 follows on from the theme in Chapter 4 and examines the relationship between executive compensation and firm performance in the GCC countries. There is an increasing interest on the ways executives are compensated and its effect on the firms' performance. The relationship between executive compensation and firm performance has been subjected to several theoretical and empirical studies providing mixed results about this relationship. To the best of our knowledge, this study is the first of its kind undertaken within the research setting of GCC region. GCC economies are generally characterised by the importance of family control, large population of expatriate executives, under-developed capital markets and relative absence of well-designed corporate governance mechanisms. These features make the GCC economic environment quite different from the Anglo-Saxon model and, therefore, investigating executive compensation within the GCC context has implications that go beyond specificities of such type of study conducted in other regions. Since the link between executive pay and firm performance represents one of the major constituents of managerial incentives for contributing to the firm growth and success, a closer look at this relationship is bound to provide much needed knowledge on the impact of executive pay on the performance of companies operating in the GCC countries.

Existing empirical studies provided mixed results on the relationship between the two variables For example, while Murphy (1985) finds a strong relationship between executive compensation and firm performance, Jensen and Murphy (1990) report only a weak association. Murphy (1985, 1999) and Coughlan and Schmidt (1985) are some of the early researchers who provided empirical evidence on the relationship. More recent studies report a weaker relationship between CEO compensation and firm performance (see for example Bebchuk and Fried, 2004; Gregg et al., 2005; Girma et al., 2007). The impact of corporate governance variables on the pay-performance relationship has also been the subject matter of many empirical studies (e.g. Marin et al. 2010; Banghoj et al. 2010; Brunello et al. 1997). Ownership structure is yet another variable that was

empirically studied to assess its impact on pay-performance relationship (e.g. Edwards et al. 2007; Ang et al. 2000; Lin et al. 2011).

The corporate governance mechanisms that could work in the context of GCC economies may differ substantially from those being applied in the Western and other advanced economies. However, there are only limited studies that focused on the impact of the governance variables on the pay-performance relationship. This is partly due to un-availability of comprehensive data and the difficulty of collecting the data from limited available sources. There are a few studies that talk about the pay performance relationship in the GCC countries (Aljifri and Mustafa, 2007; Hassan and Halbouni, 2013; Al-Swidi et al., 2012); however, they have not explicitly studied the relationship between executive compensation and firm performance. In the absence relevant literature, Chapter 5 examines this relationship in the GCC companies.

Findings of Chapter 5 show evidence of higher total executive compensation leading to better firm performance. On the other hand, we do not find any significant relationship between the components of compensation (salary and bonus) and performance. We interpret the findings of this study to point out that specific GCC economic environment and features peculiar to this region has more impact on the firm performance rather than the executive compensation.

Finally, Chapter 6 presents the overall conclusion of this research. In particular, we draw attention to the contributions of the impact of ownership structure on firm performance, the key determinants of the executive compensation and also to examine the relationship between executive compensation and firm performance in Gulf Corporation Council (GCC) countries. We also provide policy implications, limitations of the study and recommendations for further research on the topic.

Chapter 2. A Review of Corporate Governance Literature: Theory and Empirical Evidence from Developed and GCC Countries

Abstract

This paper reviews the previous literature on corporate governance to provide theoretical support to the research undertaken in the following chapters and to identify the possible research gap in relation to GCC countries. This work includes the detailed review of the findings of a number of previous studies in the related topics and the review was extended initially to the theoretical bases of the corporate governance theme as the theories were developed by academicians and scholars over different periods of time. Agency theory and stakeholder theory as they underpin the corporate governance concept was reviewed on the basis of the contribution from several research studies. The review was also extended to the broad approaches to corporate governance practices – Anglo-Saxon approach and multi stakeholder or the combined approach. As a next step in the review, a critical review of scholarly contributions to the literature about the state and progress of corporate governance practices in the emerging markets was undertaken. History of corporate governance in the GCC region and the challenges of developing a refined system of corporate governance in the countries covered by GCC were the other issues covered by this literature review. On the basis of the review of the related literature this research finds that the corporate governance practices and standards prevailing in the GCC countries are not comparable to those followed in the Western and other developed countries because of many challenges identified by previous research. Nevertheless, the review finds that there is a large scope for the implementation of globally comparable corporate governance practices in the GCC countries.

2.1 Introduction

This chapter critically reviews some of the works of researchers who have already studied the state of corporate governance and have made important observations. The researchers have focused on a wide range of aspects of corporate governance of both theoretical and empirical nature. Some researchers including Carter et al. (2002) and Fuerst and Kang (2000) have also take a region-specific approach and have compared to the growth and development of corporate governance in different parts of the world. This research focuses on the development of corporate governance in the Gulf region. However, in order to do so, it adopts a comparative approach wherein the unique aspects, advantages and limitations of corporate governance practice in Gulf is ascertained by critically comparing it to countries with alternative approaches such as Anglo-Saxon and combined or continental approaches.

This chapter contributes to this research by presenting a critical understanding of the state of research in corporate governance in general and in corporate governance in Gulf in particular. The chapter is divided into several sections. The first section focuses on the various theories of corporate governance that have evolved over the years. These theories help to understand the scope and meaning of corporate governance. The second section reviews the different approaches to corporate governance. The third section identifies the pattern of development and state of corporate governance in the developing and emerging markets. The fourth section is concerned with the critical analysis of the development of corporate governance in the Gulf region of Middle East and the Final section is concerned with critical examination of the issues in corporate governance as it is practiced in Gulf States.

2.2 Theories of Corporate Governance

One of the primary aspects of corporate governance that can be observed from the review of literature is that there has been no clear consensus about the definition of corporate governance among the researchers (Plessis, 2010). This lack of consensus originates from the difference in scope of corporate governance according to different schools of thought. These differences can be better explained through a brief review of various theories of

corporate governance. In general, corporate governance is defined as the system of tools, techniques, processes and policies that help the corporations to reach their goals with respect to different stakeholders. However, there have been some rather narrow definitions that consider corporate governance as a set of loose issues that hinder the smooth functioning of an organisation. The definition of corporate governance typically depends on the scope of corporate governance assumed by the authors (Turner, 2009). The various theories of corporate governance help to define the different levels of scope that exist in research related to this area of study. Following are some of the theories of corporate governance and the definitions that they lead to.

2.2.1 Agency Theory

Agency theory is considered as one of the original and earliest theories related to corporate governance. Agency theory asserts that there exists an agency relationship between the shareholders and the management of a company (Donaldson and Davies, 1991). In a company form of organisation, the ownership and management are separated from each other to a significant extent. A company has a large number of shareholders who may be considered the owners of the company since they provide the risk capital for the company to run. However, unlike the sole proprietorship or partnership forms of organisation, in companies the owners or shareholders do not have any control over the day-to-day decisions made. These decisions are made by professional management teams that are appointed by the Board of Directors of the company, which in turn is selected by the shareholders from among themselves as well as including outsiders. However, in spite of this absence of control over the management of the organisation the shareholders have their wealth directly dependent upon the performance and decisions of the management (Dennis and McConnell, 2003). Thus, it is naturally expected that the management would always act in the best interest of the shareholders. However, according to agency theory, there may be incentives for the management not to act in the interest of the shareholders and instead pursue their selfish ends. Thus when the interests of the management and the shareholders diverge it is stated to give rise to agency problems which in turn increase the agency costs including the costs of monitoring and costs of control (Clarke, 2004). Agency costs include those that are involved in monitoring the performance of the managers by the shareholders. However, according to Jensen and Meckling (1976) it may

be impossible to draft a contract that would take into account all possible points that could be source of agency risks in the organisations. The authors assert that due to these limitations, there are always some agency risks involved in the company form of organisation. Accordingly, the corporate governance tools, techniques, policies and procedures are intended to minimise the agency costs in the organisations. Thus the scope of corporate governance, according to agency theory, is limited only to the relationship between managers and owners of the company.

According to agency theory, corporate governance revolves around the problems of agency and includes all the policies and tools that are used by the organisation to align the interests of the shareholders and the management so that the organisation would continue to function in the best interest of its shareholders (Harris and Raviv, 2008). One of the most important aspects of agency theory is that it restricts the scope of corporate governance only to the extent that the interests of the shareholders are protected and taken care of. Over the years, the advocates of agency theory have developed several solutions to mitigate the agency risks caused by the separation of ownership and control in companies. It is stated that nature and structure of executive compensation could be a very important and useful tool in minimising agency frictions (Blair, 1995). The companies have widely adopted the practice of linking the performance of the company to the management incentives so that the managers would have an explicit interest in maximising the performance. However, it is observed that this could also give rise to accounting and performance manipulations and in some, even to acute scandals and scams in the organisations. Due to these reasons, it is seen that the performance incentives of the senior management is tied to the long-term performance of the organisation in the form of issue of stock options. Using this tool, it is seen that the predominant portion of the private wealth of the managers is accumulated in the form of shares of the company for which he works and so he has a vested interest in ensuring that the company not only earns above average profits in the short term but also manages to sustain a high profitability level over the years.

Several researchers have supported agency theory on the basis of the advantages or strengths of the theory. Donaldson and Davis (1991) note that agency theory has led the corporate world to identify some important tools to minimise the friction in the organisation. The authors note that agency theory is important because it has the potential

to result in very useful and highly application oriented solutions. According to the authors, performance-based incentives, stock option plans and non-cash bonus, board independence, audit committees are important inventions made over the years using agency theory as the basis. Yermack (1995) asserts that vesting period included in the stock options have helped the companies to link the personal wealth of the managers to the long term performance of the organisations and so it has yielded desirable effects. Harris and Raviv (2008) observe that the agency theory presents an important and functional framework for the institutional investors to identify ways of improving the overall standard of governance in a corporate organisation. Agency theory has demonstrated that gaining control of the Board through appointment of directors may be able to provide the large institutional investors the ability to control the performance of the management. Ahmed and Duellman (2007) show that the companies in which large institutional investors hold significant stakes typically have a better system of governance and lower agency costs than the other companies.

Even though agency theory is arguably one of the widely accepted theories in corporate governance, it is seen that several researchers have criticised the theory for its myopic view of corporate governance as well as the scope for misplaced incentives. Driver and Thompson (2002) argue that the agency theory may not be suitable for an organisation from a long-term perspective because the agency theory is all about caring only for the shareholders. The authors argue that a successful organisation requires contribution from a wider range of stakeholders and so the interests of all these stakeholders should be served by the organisation so as to attain a level of sustainability. This is one of the most common arguments against agency theory. Some researchers including Blair (1995) and Heath and Norman (2004) have identified some technical issues in agency theory. According to these authors, the primary premise that shareholders are the owners of the company is itself is not completely tenable. The authors assert that an owner should be able to not only enjoy the returns from the business but also should be able to exercise control over the operations. However, in the case of companies only the major shareholders may be able to exercise some control over the organisation through their directorships. The small or minor shareholders, if they are not satisfied with the performance of the management, have to either continue to tolerate the performance or have to exit the company by selling off the shares in the secondary market. Therefore, technically it is not appropriate to equate the shareholders to the owners of the companies.

This difference between the major and minority shareholders in terms of their ability to exercise control over management is referred to as the Principal-Principal problem by Young et al. (2008). These are some of the major limitations of agency theory, as identified by the researchers.

2.2.2 Stakeholder Theory

Stakeholder theory is presented as a popular alternative to agency theory. The proponents of stakeholder theory argue that agency theory takes a very narrow approach to corporate governance (Donaldson and Preston, 1995). The stakeholder theorists claim that the organisation has responsibilities not only towards the shareholders but also towards a wide range of agents in the economy including the customers, suppliers, employees, environment, society, government, communities, etc. Therefore, according to the stakeholder theorists it is essential for the management of the organisation to take into account the interests of all these diverse group of audiences while making the decisions (Driver and Thompson, 2002). Thus, stakeholder theory asserts that the value of an organisation is maximised when it fulfils its responsibilities towards each one of these groups of stakeholders. A stakeholder of an organisation is defined as any entity that is affected by the performance and existence of the organisation.

Stakeholder theory posits that corporate governance includes the set of all policies and systems that ensure that the organisation functions in the interest of all its stakeholders. OECD's definition of corporate governance that "Corporate governance involves a set of relationships between a company's management, its board, its shareholders and other stakeholders" is one of those that are rooted in the stakeholder theory (Chapman, 2006). It is noted that the multilateral and government agencies typically adopt a stakeholder view to corporate governance.

In general, it is seen that the scope of corporate governance during the initial days was limited only to finding solutions to and avoiding agency problems due to which agency theory was considered the most appropriate. However, as the roles of organisations have widened from a social and community perspective the stakeholder theory has gained popularity and most of the recent researchers broadly adopt the stakeholder approach.

Kulik (2005) argues that stakeholder approach is more relevant than shareholder approach or agency theory approach because shareholders are also considered one of the several groups of stakeholders. Thus, the stakeholder theory helps to widen the scope of corporate governance and is also highly flexible in nature. Mahoney (2006) argues that the issue concerning the ownership rights of shareholders, which is present in agency theory, can be resolved using stakeholder theory. According to Mahoney (2006), the shareholders, much like the other stakeholders, contribute towards the survival and growth of the organisation and so the company owes certain obligations towards the shareholders. Thus according to the author, the issue of differences between shareholders and owners, as pointed out by Blair (1995) and Heath and Norman (2004), may not be present in stakeholder theory.

There have been some issues with stakeholder theory identified by the researchers. Sternberg (1997) argues that stakeholder theory gives rise to conflicts between the interests of different stakeholders. According to the author, "balancing stakeholder interests is an ill-defined notion, which cannot serve as an objective performance measure". Vos (2002) too notes that the interests of different groups of stakeholders are complex and intermingled in nature. If the management were to focus on fulfilling the interests of all stakeholders, then it would lead to confusion and poor performance on the part of the management. The problem of complexity arises right from the definition of stakeholders (Sternberg, 1997). The word stakeholder may refer to a wide range of individuals and organisations within the ecosystem of the organisation and so it would be almost impossible to create performance targets to fulfil the expectations of all these different stakeholders. These are some of the practical issues involved in the application of stakeholder theory.

2.3   Corporate Governance Approaches

From the previous section, it is noted that the definition of corporate governance has varied on the basis of the scope of corporate governance, which in turn is dependent upon the theory or school of thought that the researcher adopts. On the basis of evolution, corporate governance is observed to have two different approaches. This section is concerned with the review of literature that has focused on the different approaches of

corporate governance. This is critical as the next section focuses on the differences between these approaches, which in turn are used as the basis for narrowing the focus on corporate governance in Gulf. There are two broad approaches that have been evolved – the Anglo-Saxon approach and the combined approach.

2.3.1 Anglo-Saxon Approach

The Anglo-Saxon approach has had its origins in the Anglo-Saxon countries including the UK, the US, Canada and Australia. This approach is very closely related to the agency theory of corporate governance. According to the Anglo-Saxon approach, the focus of corporate governance is on protecting the interests of the shareholders of the organisation (Garcia et al., 2008). They recognise shareholders as the owners of the company whereas the management is appointed to ensure that the company generates wealth for the owners. Capital is considered the primary source of wealth and all other factors of production are acquired using capital as the base. Thus, the business exists to promote the interest of the capital providers. The Anglo-Saxon approach has a strong foundation in the capitalist principles and policies. Due to this reason, it is noted that most of the countries that have adopted original forms of capitalism have also embraced the Anglo-Saxon approach to corporate governance. As stated earlier the critics including Kulik (2005) and Driver and Thompson (2002) argue that considering an organisation's sole purpose of existence is to add value to the shareholders is too narrow in scope and limits the roles of large organisations in the social framework.

Anglo-Saxon approach relies on free market as the correction mechanism. When an organisation has a very high level of agency risk, the agency costs increase for the organisation as a whole due to which the market price of the shares of the company sees a decline to account for these costs (Moerland, 1995). This makes the company an attractive target for takeover by other players in the industry. Thus, there is a strong incentive for the company to work towards minimising the agency costs so as to ensure survival and growth of the organisation. The market mechanism is also expected to work through adjustments in cost of capital. Companies with very weak corporate governance and high agency risks typically see a high cost of capital and the financiers take into account the agency risks and its impact on the bankruptcy costs of the organisation

(Williamson, 2002). The high cost of capital is expected to make marginally profitable projects unviable and also is expected to cut down the profitability of the other projects. Overall, it is expected that market mechanism translates high agency costs into weak financial performance.

2.3.2 Combined Approach

The alternative approach to corporate governance that has been adopted in a number of European countries including Austria, Germany, France and Italy is the combined governance approach or multi-stakeholder approach. According to this approach, corporate governance is concerned with ensuring the company performs its rightful duties towards different stakeholders in an appropriate manner (Herrigel, 2008). The various corporate governance mechanisms are instituted in order to monitor the performance of the organisation from the perspectives of different stakeholders and to make changes as required. It is noted that the combined approach takes a strong base in the stakeholder theory of corporate governance and hence corporate governance in a much broader manner in comparison to the Anglo-Saxon approach. Even within the combined approach, there are several models with some variations. These include the Japanese model, French and German models.

2.3.2.1 The Japanese Model

The Japanese model of corporate governance is considered the closest to the stakeholder theory as various groups of stakeholders are given importance (Allen and Zhao, 2007). It is seen that the Japanese system of corporate governance is based on traditional and familial values as the businesses were originally run by families. The shareholders typically have a long-term focus. Yafeh and Yosha (1999) note that a typical shareholder has a tendency to hold on to a stock for about 8 years. Therefore, the decisions made by the managers are expected to be focused on adding value to these shareholders. The managers are expected to be loyal to their shareholders and so no elaborate system of incentives exists for managers. Yafeh (2000) notes that the market for corporate CEOs is non-existent in Japan as the CEOs typically rise through the ranks in the same

organisation and direct CEO appointment are extremely rare in Japanese corporation. The focus of the CEOs is on wider range of stakeholders rather than singularly on the shareholders.

2.3.2.2 The French Model

The French corporate governance model is focused on the welfare of the employees as much as the shareholders of the companies. The strong labour laws and the natural affinity towards Marxist principles are considered the foundation of such a labour-oriented corporate governance system in France (Morin, 2000). It is noted that the trade union movements have traditionally been strong in French corporate world and in some cases, the union members have even had representation on the Boards of the companies. However, Goyer (2003) notes that during the recent years, there has been major movement away from the original French model towards the Anglo-Saxon model. The author attributes this to the growing dominance of the American and English financial institutions in the capital market in France. It is estimated by that the author that about 40% of the equity of topmost companies in France is owned by these financial institutions due to which the corporations have been in a way compelled to adopt Anglo-Saxon principles. Thus, according to Goyer (2003) the modified French model is actually a mixture of Anglo-Saxon model and the original French model.

2.3.2.3 The German Model

The German model places more emphasis on the labour or employees as the most prominent group of stakeholders and so these models require that the management should make its decisions on the basis of the likely impact of the decisions on the employees of these organisations (Driver and Thompson, 2002). The German model is based on 'co-determination' which has been included in the constitutional law as well. In the German model, there is a two-tier system for management wherein the Board is supplemented by a works council, which comprises of the representatives of the labour force. Goyer (2003) observes that during the recent years the Anglo-Saxon model has dominated the German model as well as most of the multinational corporations in Germany have moved formally

towards a system, which is more dependent upon the market and is more focused on the shareholders than the other groups of stakeholders.

Many researchers including Jones and Pollitt (2003), Clift (2007), Suchan (2004), Cernat (2004) and others have observed that during recent years there has been narrowing in the gaps between different approaches to corporate governance. It is noted that most of the countries with combined approaches have shown a tendency to move slowly towards the shareholder-friendly policies and frameworks. In effect, most of the countries have adopted the Anglo-Saxon model to some extent at least. Klapper and Love (2004) note that the developed markets such as the US typically have a strong legal system coupled with superior enforceability standards due to which the regulations of corporate governance could be enforced in spirit. Most of these authors have attributed this change to the success of the corporate governance model in the US in promoting and prosperity in the economy and the society.

2.4   Overview of Corporate Governance in Emerging Markets

It is essential to study the state and progress of corporate governance in emerging markets around the world because it may be reasonable to expect that there could be similarities between the corporate governance in Gulf and the emerging markets. One of the most common patterns of corporate development in both Gulf region and the emerging markets has been the dependence on external capital. A brief review of corporate governance practices in emerging markets may help to compare them to the Gulf countries' as well.

Aguilera et al. (2011) trace the development of corporate governance in six emerging markets around the world. The authors argue that the development of governance practices depend upon the changes in the ownership patterns in these countries. The authors compare the ownership patterns of companies for six countries - Brazil, Chile, South Korea, Czech Republic, Hungary, and Poland in the 11th century and in late 19th century. The authors conclude that "although concentration of corporate shareholdings continues to be a common denominator among these emerging countries, the processes and structures controlling firms across countries is remarkably different". In some countries, the process of privatisation was the trigger to development of corporate

governance policies and practices. According to the authors, as the percentage of ownership of retail investors increased in these countries, the governments stepped up efforts to protect the interests of the retail investors through creation of appropriate corporate governance mechanisms and regulations. Specifically, it is stated that the increase in the concentration of the institutional investors catalysed the process of governance development in some of these countries. From this research, it is evident that privatisation and ownership patterns are two of the major factors that have shaped the development of corporate governance in most of the emerging markets.

Young et al. (2008) note that there is a unique issue that is evident in the development of corporate governance in the emerging markets. The authors state that it is common for the governance to be centred on the principle-agent relationship, in emerging markets there are issues related to principal-principal relationship. The principal-principal relationship issues emerge between the controlling shareholders and the minority shareholders. The controlling shareholders typically attempt to ensure continuity of their control or to increase the strength of control by appointing powerful directors to the Board. The minority shareholders have limited exposure to the affairs of the Board. It is observed that the emerging markets typically have weaker corporate governance policies such as extensive family ownerships, business group structures, weak legal protection of minority shareholders, etc. Khanna and Palepu (1999) trace the development of corporate governance in developing markets through a case study analysis of India. The authors note that an increase in foreign institutional investors leads to an improvement in the state of corporate governance in general. The companies with higher concentration of foreign ownership have better governance practices. Further, affiliation of companies to business groups lead to weaker governance structures in these companies. Also, it is noted that such companies attract less investment from foreign investors. They conclude that, "groups are difficult to monitor, and that foreign institutional investors serve a valuable monitoring function as emerging markets integrate with the global economy". An important role of foreign institutional investors that Khanna and Palepu (1999) identify is that they help to bring the best practices in corporate governance to the emerging markets from the developed markets around the world. Thus, the foreign institutions play the roles of conduits, which is critical to development of governance practices in emerging markets around the world**.** One of the most important points to be drawn from

this research is that the foreign institutional investors play constructive roles in corporate governance development.

Klapper and Love (2004) find a strong relationship between corporate governance standards and the strength of legal systems. Due to this reason, the authors argue that the emerging markets typically have weaker corporate legal systems than the developed markets and so the enforceability of the governance standards is weaker in the emerging markets. This is a critical point in the context of this study as legal systems in Gulf countries are unique in that they follow the Islamic laws, which are quite different from the laws in Anglo-Saxon countries or the developing countries. Klapper and Love (2004) also find that there is a very strong correlation between the operating performance and market valuation. The firms with better operating performance and high market valuation typically tend to have strong corporate governance policies and practices than the firms with weaker operating and financial performances. The authors find this classification to be true in various developing countries. It may be reasonable to expect this difference to exist even among the firms in Gulf economies. Klapper and Love (2004) argue that the corporate governance policies and provisions matter most in markets with weaker legal environments than those with stronger ones. These are some critical points that could be of importance to this research due to the unique nature of legal systems in the Gulf economies. Even though the Gulf economies have a legal system that is largely based on the Islamic laws, it is seen that these laws are not specific to the corporate environment and most so most of legislations and laws related to corporate are derived from the general laws. Thus, by applying the argument of Klapper and Love (2004) to Gulf economies, it can be inferred that the corporate governance standards matter most to these economies due to their generally weak system of corporate laws.

Gibson (2003) analyses the development and the state of corporate governance in the developing markets. Using a sample of such markets the author observes that the corporate governance standards in these markets cannot be stated to be weak as it is generally observed that the CEOs in the companies in emerging markets are more likely to lose their jobs than their counterparts in developed markets if the firm performance is poor. On this basis, the author argues that the corporate governance should be stated to be effective in the developing markets in general. However, the author finds that in a sub sample of firms in developing markets where the domestic investor base is very large,

there is clearly no link between the CEO turnover and the financial performance of the firms. Therefore, the author concludes that in firms with large domestic investor stake holding the corporate governance standards may not be as high as it is observed in the other firms within the developing markets. This is yet another research, which clearly establishes the importance of foreign investors in the effective functioning of the corporate governance mechanism in developing, markets in general.

Fan and Wong (2005) accept that one of the major issues in corporate governance in emerging markets is the lack of compatibility between the large shareholders and the minority shareholders. The authors enquire whether such firms in emerging markets using the external auditors as important binding mechanisms to bring together these two groups of shareholders. Using a sample of emerging markets in East Asia, the authors note that the firms with large agency issues stemming from the ownership patterns are more likely to hire one of the top 5 audit firms in the world. More importantly, it is also noted that such firms that hire very popular audit firms tend to experience very small discounts in relation to their agency conflicts. The authors go even a step ahead and argue that the audit firms fix their fees taking into account the possible issues related to agency conflicts and ownership patterns in their client companies. Thus according to Fan and Wong (2005) the top audit firms have very important and critical corporate governance roles in the emerging markets. This is a critical point, which may make it useful to enquire into the choice of auditors of the firms in Gulf markets.

From the review of literature related to the development of corporate governance in the developing or emerging markets it is noted that the emerging markets have seen strong development of corporate governance on the basis of the overall improvement in the corporate environment. However, most of the researchers have found the corporate governance standards in these countries to be less developed than those in the developed markets.

2.5   History of Corporate Governance in Gulf Region

The previous sections of this chapter have performed a critical analysis of the literature related to the two different approaches to corporate governance, the popular theories underlying the concept and the development and state of corporate governance in the emerging markets. However, the main area of interest for this research is corporate governance in gulf region.

There are some researchers who have focused on the development of corporate governance in the Middle East or Gulf regions. Naciri and Naciri (2008) observe that the corporate governance systems in Gulf markets have been of recent origin. The author notes that during the initial years the corporate sector in these economies has been dominated by the presence of governments. The national and the regional governments had been the sole or major shareholders in most of the businesses during the initial years due to which there was no major need for corporate governance that was felt. The governments had appropriate departments to oversee the operations of these companies and these departments had absolute control over the appointment of the management teams and the senior professionals within the companies. The management team was directly responsible for the performance of these companies. However, the authors note that as the corporate sector entered into the second level of development the traditional family wealth was redirected into the corporate sector. During this period, there was a huge development in this sector as the families in Gulf region came forward to become owners of some of the large businesses. The authors point out the fact that the family ownership is mostly passive in nature and the families do not tend to sell off or reduce their stake in these companies. The need for corporate governance was started being felt during this period as the families of investors were not actually well-versed in the technical details of these businesses and so they relied largely on the knowledge and skills of the professional managers to conduct the affairs of the business. Thus, the separation of the ownership and control actually came into being. Naciri and Naciri (2008) note that most of the large businesses in Gulf region continue to be owned by the families in the region. Due to this reason, there has only been a moderate need for corporate governance that has been felt by the economies. Even though the ownership and control are mostly separated, most of the directors work in perfect harmony to protect the interests of the

largest shareholders and so there are strong practices that are generally adopted to ensure that the governance standards are good enough to protect the shareholders' interests.

Al-Zuhair (2008) also acknowledges that the corporate governance development in Middle East in general has not been at desirable levels. However, the author brings focus to the fact that there are some pockets of strong corporate governance that have emerged from some of the countries in the Gulf region. The author refers to the free zones such as Dubai International Financial Center (DIFC) and Bahrain Financial Harbour (BFH), which have strong corporate governance standards for the members within. One of the reasons the author identifies as to which such high standards have not generally been adopted by regulators outside these independent free zones within these Gulf countries is that the corporate sector and the capital markets outside these free zones are not as developed as they are in the developed markets. Therefore, according to Al-Zuhair (2008) there is actually no need felt for developing the corporate governance standards of global level in the markets in the Gulf region. However, the free zones, which the author identifies, are created with the core intention of attracting some of the largest financial institutions from around the world and so it is essential for the regulators within these free zones to create a regulatory environment that is as safe and secure as the ones that are found in the native countries of these institutions. Due to this reason, the corporate governance standards enforced within these free zones are of very high standards that are comparable to the standards in the developed markets. Rehman (2010) notes that there is an increasing tendency of growing importance of institutional investors in the companies in Gulf region. The author points to the fact that the flow of foreign capital into the companies in the region through institutional route has been increasing during the recent years. One of the well-established observations which Rehman (2010) refers to is that such a steady increase in the interest of institutional investors from abroad on the companies in Gulf could lead to stronger governance standards among the companies. The author argues that the weak and under developed nature of the corporate debt market in Gulf region has meant that almost all the capital needs have to be met through the equity market and so this has attracted the foreign investors as the leverage position of the companies in Gulf have been typically low. Further, the large businesses in the Gulf region enjoy the support and patronage of the governments in their countries and so the foreign institutions find it more secure to infuse capital into such businesses.

These research papers show that the corporate governance scenario in the Gulf region may vary from one country to another but typically has sufficient scope for further progress and development. It is also noted that there are some pockets of strong governance that have emerged within the Gulf region. There is also found to be a very strong relationship between the pattern of development of governance and the ownership structure in general.

2.6   Corporate Governance Practices in Gulf Region

The previous section has discussed the general development of corporate governance in Gulf region. This section specifically focuses on identifying some of the distinguishing factors of corporate governance in the Gulf region. This section also attempts to identify some of the major issues related to corporate governance, which could be considered important areas of future growth in Gulf region.

2.6.1   Corporate Governance Practices and Development

Faras and Ghali (2009) note that the Gulf region, commonly referred to as the Gulf Cooperation Council (GCC) region, has seen tremendous economic growth during the last decade. As the crude oil prices have hit record highs and the influx of the foreign investments have increased, the stable members within GCC have seen steep growth rates on a consistent basis. Economies such as Kuwait, UAE and Saudi Arabia have remained politically stable and so have seen some major developments. Several researchers including Harb (2009) and Weir (2011) have shown that corporate governance is on an increase in importance in GCC states. However, one of the most important aspects about the nature of business environment in GCC states is that most of the businesses, even the largest corporations, continue to be held mostly by families and governments. This closed control structure means that these companies typically do not have any external shareholders or even if they have external shareholders the stake that is diluted to the external shareholders is only minor. Due to this reason, the families and the governments have continued to remain in absolute control of the companies. Another important feature of the business environment in GCC economies is that the capital markets are not very

well developed. The capital markets have continued to remain much smaller and the regulatory structures still have a long way to improve. The nascent state of capital markets may be attributed to the general lack of dependence of the businesses on external capital. Instead, these businesses tend to rely on their internal reserves or government funding for expansion and growth. Due to these reasons, the corporate governance structures in GCC economies have largely remained at nascent stages.

The state of corporate governance in Saudi Arabia largely falls in line with the general trend in the GCC region. Saudi Arabia's market regulatory – Capital Market Authority (CMA) issued the first set of regulations on corporate governance in 2006, as it was realised following the steep decline in the stock prices that the regulator needs to put forth a better system for transmission of corporate information to the shareholders of the listed companies in the market (Solomon, 2007). The regulations were based on the Capital Market Law, which is the central legislation for control and regulation of listed companies in Saudi Arabia and the regulations were passed by the Royal Decree no. M/30. In 2009, these regulations were amended by the resolution of the Board of Capital Market Authority. These regulations, along with amendment resolution, have been the cornerstone of the corporate governance in the country during the last 5 years. The regulations spell out the provisions related to rights of shareholders and the general Assembly of the companies, disclosure and transparency, Board of Directors and closing provisions (Capital Market Authority, 2006). The part on Board of Directors is considered the most important and it includes detailed provisions related to functions of the Board, responsibilities, formation, committees, remuneration and handling of conflicts of interests of the Directors in general.

Ulrichsen (2011) notes that during the recent years, the GCC states have been more prominent in the international arena. These states have engaged in a closer level of cooperation not only with the developed economies but also with the emerging economies at a political and economic level. The author however notes that the cultural and religious aspects have remains largely local and the GCC states have not come forward to adopt a broader international perspective in these areas. However, notwithstanding this limitation the cooperation levels have increased tremendously. The author argues that adopting strong corporate governance standards could contribute significantly towards further strengthening of ties and relationships of the GCC states with the global economies.

However, the author raises an issue that corporate governance has a strong relationship with the local business environment and the ownership patterns. The author notes that these aspects are quite different in the Gulf States when compared to the other countries from developed and developing regions of the world. Due to this reason, Ulrichsen (2011) shows some suspicion towards the possible extent to which the GCC states may be able to integrate themselves with the global business and governance practices.

Darrat and Al-Shamsi (2005) note that the six economies in the GCC have highly integrated and similar financial and political structures that mean that these countries can come together even further and form a common economic region as Euro region. The authors refer to the fact that several efforts have already been undertaken by the rulers of these states to forge stronger economic and financial ties among these countries. However, the authors note that one of the important areas where there are notable discrepancies is corporate governance. The authors find that generally some countries including UAE and Bahrain have much higher standards of corporate governance than other countries in the Council. Due to this reason, there is a need for these countries to reconcile their differences and ensure a uniform system of corporate governance among all the members. According to the authors, a unified economic region would require a unified regulation for the capital markets in the region. As the capital markets come together, the governance standards for corporate also should converge in order to ensure that there are no corporate governance arbitrages within the region. Thus according to the authors a strong and unified system of corporate governance is an essential aspect of ensuring a strong system of co-operation among the members of the council. The authors also suggest that in order to improve the overall standards of corporate governance within the Council, the regulators may either adopt the systems that exist in practice in the stronger countries within the Council or can adopt a better learning approach by adopting stronger policies from outside the Council. Even though both are expected to lead to overall improvement in the governance standards, it is stated that the latter model could lead to even stronger developments and progress.

2.6.2 Corporate Governance Issues in Gulf

Even though the corporate governance laws and systems are of recent origin in GCC, several researchers have identified some major problems with the state of corporate governance and the regulations governing them. World Bank (2009) in its Report on the Observance of Standards and Codes (ROSC) on Corporate Governance in Saudi Arabia observes that the standards and the regulations in Saudi Arabia in relation to corporate governance has been generally in line with the best practices adopted by other countries around the world. However, the report states that the regulator needs to perform a better job in implementing these provisions. One of the biggest issues with the regulations as they stand at present is that they do not specify any punishments or fines for failure to adhere to the provisions mentioned. Therefore, there is a very high degree of subjectivity involved in the implementation of the provisions by the officials and the authorities, which in turn dilutes the purpose of these regulations. The World Bank also notes that the introduction of the corporate governance regulation is only the first step in the three-step process of ensuring corporate governance in the market. The second step that has been suggested is that the regulator should work towards increasing the level of knowledge and awareness among the market participants and the companies about corporate governance and the importance of adhering to very high governance standards. The final step would be the introduction of strict enforcement standards for the corporate governance regulations. Thus, according to World Bank, the regulator still has a very long way to go in reaching world-class corporate governance in Saudi Arabia.

Weir (2011) notes that the corporate governance and transparency in Middle East countries is typically below the level observed in other developing countries around the world, particularly in Asia. The author attributes this situation of low corporate governance standards to a host of factors. He observes that the education level in Saudi Arabia and other neighbours is typically below par when compared to European and American countries. It is also seen that the institutional investors have very small roles in the capital markets in countries like Kuwait and Saudi Arabia. Typically, institutional investors are considered champions of governance in companies and so the lack of power for the institutions has inhibited the growth of corporate governance in the countries. Further, the author also notes that the governments as well as the corporations act in a highly mysterious manner with very little information shared with the public. The excessive control over media and the absence of freedom for press mean that the shareholders may not have access to the kind of information which the Western media

may be able to publish about the internal affairs in the corporations. It is also argued that the lack of investor activism and the excessive government involvement in the corporations may also be hindering the progress of corporate governance in countries such as Kuwait and Saudi Arabia. These are some of the major issues related to corporate governance that have been identified by Weir (2011).

Raphaeli and Gersten (2008) focus on the Sovereign Wealth Funds (SWFs) and argue that the corporate governance standards adopted by these funds should be improved so as to lead to more transparent and better-informed investments around the world. The authors note that even though China, Norway and Singapore too have active SWFs, the SWFs of the countries in the Gulf region are considered more important and are often talked about in the international arena because of the tendency of the Middle East SWFs to invest in businesses that are located in more developed economies such as US and UK. One of the important aspects of the investment patterns of these SWFs is that they at times exhibit a behaviour, which may not be justified entirely from the investment perspective. Therefore, the authors argue that there is a general fear among the retail investors and minority shareholders in the developed markets that the entry of such SWFs from Gulf region could lead to dilution of the overall standards of governance. Raphaeli and Gersten (2008) argue that one of the most important ways in which these SWFs may be able to establish their intent is by adopting a better system of corporate governance. However, the countries in which they are incorporated do not have strong governance standards and so technically these SWFs themselves are not required to adopt better governance standards. Therefore, according to Raphaeli and Gersten (2008) the real problem lies in the overall poor corporate governance standards in Gulf region. The authors argue that in order to pursue investment opportunities these SWFs should either voluntarily adopt the higher standards of corporate governance that are prevalent in the countries where they make their investments or the overall standards be elevated in the Gulf region as a whole. The authors note that either way it is imperative for the SWFs to become more transparent in their operations so as to overcome the wide spread fears of governance and ethical deficits.

2.6.3 Empirical Research on GCC Countries

Alsaeed (2006) undertakes an empirical research to study the level of voluntary disclosure of information related to corporate governance by Saudi listed firms. The author identifies a set of 20 voluntary items and uses a sample of 40 firms to determine the level of disclosure. The author notes that the level of disclosure is generally below par and the companies are typically not interested in providing even those information that are considered critical in other regulatory regimes. The author presents an opinion that "The outcome of this study is undoubtedly of great concern to the investment community at large to assist in evaluating the extent of voluntary disclosure by Saudi firms and explaining the variation of disclosure in light of firm-specific characteristics" (p. 476). This research evidently shows that the disclosure standards in Saudi are very low and are not at desirable levels. On one hand, this shows that the present corporate governance standards are not at globally expected levels and on the other hand reveals the significant scope that is available for companies to add value to their shareholders through additional disclosures.

Sourial (2004) studies the state of corporate governance in Middle East and North African (MENA) region and focuses on eleven countries in the region. The author notes that the market structures in these countries have undergone significant developments during the last decade. However, the author observes that there is a significant gap between policymaking and implementation in the soft areas such as corporate governance in general in all these countries. The author brings in a very interesting perspective and notes that most of the corporate governance standards are borrowed from the Anglo-Saxon models. However, it is stated that the problem with these standards is that they do not comply with the cultural and societal values of the people and companies in this MENA region. Therefore, there are problems involved in implementation of these standards. On the basis of this issue, the author suggests that the MENA region countries should attempt to develop their own standards of corporate governance which are based on Al-Sharia rather than borrowing from Anglo-Saxon models. According to the author, the present state of corporate governance in MENA region economies is below expectations.

Bhatti et al. (2006) focus on the attractiveness of Dubai as a destination for the international businesses. The authors note that Dubai had seen rapid development within

UAE and even within the GCC region during the last few years. One of the reasons that the authors identify is that the emirate has adopted a stronger structure of corporate governance for the international businesses that are located in the free zones. The authors note that there are several free zones that are located within the emirate and each free zone typically has an independent regulator who is separate and detached from the Federal regulator in terms of adjudication and policymaking powers. The authors observe that the corporate governance procedures and policies required for compliance with the regulations within the free zones in Dubai are much tougher and stricter than those that are typically followed within the GCC region. Due to this reason, the international businesses particularly the institutional investors have found it more compelling to incorporate themselves within the free zones within Dubai. The authors use this case study as an example to demonstrate that the international institutions are focused strongly on better corporate governance and so in order to attract them it is essential for the Gulf regional economies to ensure that they create a strong system of corporate governance and legal enforceability to support the governance standards.

Al-Shammari and Al-Sultan (2010) study the relationship between corporate governance and voluntary disclosure by firms listed on Kuwait Stock Exchange. The authors first identify four major corporate governance attributes that may be highly relevant to the firms in Kuwait – "proportion of non-executive directors to total number of directors on the board; proportion of family members to total number of directors on the board; role duality; and a voluntary audit committee" (Al-Shammari and Al-Sultan, 2010: p. 262). The authors use these factors to measure the level of voluntary disclosure by the Kuwaiti listed firms. It is noted that during the two years between 2008 and 2010 the level of voluntary disclosures increased from 15% to 19%. Of the various factors, it is observed that the presence of an audit committee is positively and significantly related to the level of voluntary disclosures made by the companies. This observation is found to hold valid after controlling for changes in various aspects including company size, leverage, auditor type etc., On the basis of the observations made from empirical research the authors conclude that it may be possible to improve the overall standards of corporate governance in Kuwait by enforcing some more important changes such as mandatory requirement for audit committee. The authors present these as suggestions to the regulators in Kuwait. Even though the sample is drawn from among the listed firms in Kuwait, the authors

argue that the suggestions may be in general useful to improve the corporate governance standards in other members of the GCC as well.

Adawi and Rwegasira (2011) study the determinants of strong voluntary corporate governance practices among the listed companies in UAE. The authors observe that UAE in general has a fairly unique corporate governance environment within the Middle East as the companies are expected to adhere to higher standards in UAE. However, the authors find that the existing system of mandatory requirements related to corporate governance could be still inadequate when seen in the global context. The authors attempt to identify the factors that compel the companies in UAE to voluntarily adopt better governance practices that those mandated by regulations. The authors find that the quality of the corporate Board is critical to the level of voluntary adoption of corporate governance. Specifically it is noted that the Board with more directors, diversified set of directors and more experienced directors tend to voluntarily adopt better corporate governance practices that the companies within weaker Boards.

Safieddine (2009) studies the practice of corporate governance in Islamic Financial Institutions. The author observes that the typical ways of managing the agency problems in corporations may not be applicable in these Islamic institutions due to the fact that these tools may not be compliant with Al-Sharia. It is seen that the corporations in the Anglo-Saxon countries use stock options as an effective way of bridging the gap between the interests of the shareholders and management. However, stock options may not be valid in Middle East markets including Saudi Arabia where issuing derivative instruments on the basis of financial claims and intangible ownerships are considered as non-compliant with the Sharia laws. Therefore, there is a strong need to identify alternative ways of enforcing corporate governance in the Islamic institutions and corporations that are founded on Islamic principles in countries such as Saudi Arabia and Kuwait. The author observes "some governance flaws relating to audit, control, and transparency" (p. 142). The author notes that it could be challenging for the regulators in Islamic countries in Gulf to develop an effective and enforceable governance standards framework while also ensuring compliance with the principles of Shariah.

2.6.4 GCC and the Global Recession

Different countries, co-operations and organisations responded to the global economic crisis in different ways. Most commonly, the response given to the recession had to deal with the specific crisis that these countries, co-operations and organisations faced as individual entities in the entire crisis session. In the Gulf regions and specifically with the GCC Countries, there were varying effects of the crisis on companies and governments. For instance just as prices of oil, natural gas and other commodities produced in the Gulf region began to rise to the advantage of the cooperation in the first half of 2008, governments and companies also had to deal with rapidly rising food and raw material prices that threatened their economies and social stability (Rivlin, 2009). In the quest of reviving the economies by making provision for supply of food and raw material with revenues from oil and natural gas, the region eventually saw the decline of oil and natural gas as a result. The effects did not end there as Rivlin (2009) documents that "Arab oil exporters experienced a fall in hydrocarbon receipts, deterioration in their terms of trade, and declining surpluses on their balance of payments."

Notwithstanding, the impact and extreme crisis faced by the Gulf region, there were proactive reacts to help curb the effect of the global economic meltdown. The reaction of the Gulf region was so massive and glaring that it was noticed and acknowledged by global organisations such as the International Monetary Fund. In the estimate of the International Monetary Fund (IMF), "the GCC countries confronted the global crisis from a position of strength." The International Monetary Fund in effect identifies two major reaction models adapted by the regions. In the first place, there was massive "focus on clean-up of bank balance sheets, restructuring nonbanking sector" (IMF, 2010). Through banking and nonbanking reforms that were initially seen as harsh, the IMF (2010) observes that "the measures adopted by the authorities enhanced the sector's stability and the public's confidence in it." Because of the confidence the public entrusted in the banking sector, investment among most companies including oil companies was shifted from the usual quest for oil into financial investment. For this reason, "banks continued to post profits throughout the crisis, and overall, the impact was moderate" IMF (2010). The second reaction as noted by the IMF (2010) was "greater transparency, stronger regulatory framework needed over long term." This means that governments started preparing for the future right in the midst of the crisis. The strategy for growth was

creating a sense of trust and transparency among investing companies so that they would have faith in the governance and economic hospitability in doing business in the region.

It has already been mentioned that the main challenges to corporate governance in the Gulf region are related to raising awareness and creating a comprehensive corporate model, which would attract foreign investment and enhance regional economic development. Other problems are related to transparency and accountability, as well as business ethics. The combination of these factors has affected individual firm performance in the region, as well as its overall economic performance. The measures against the recession, taken by the national governments in the Gulf region have been related to re-directing investments to other areas such as tourism, agriculture and the financial services. The rationale behind these measures was to cut the Gulf Countries' dependency on oil, and to present expanded market opportunities for existing corporations. Yet it is difficult to trace a unitary mechanism for fighting the global economic recession in the case of the GCC because the economic setting and wealth vary from country to country. For example, the main strategy of the government in the UAE was to inject funding into five of its main banks, in order to secure that the banks will cope with tight credit conditions (Saif and Choucair, 2009; Baydoun, Ryan and Willet, 2013). In Kuwait and Saudi Arabia for example, the main strategy adopted by the government in curtailing the effect of the recession is mostly related to preserving their conservative monetary and fiscal policy, and restriction of internal capital flows from foreign investor. Saif and Choucair (2009) point out that Oman and Bahrain have followed an entirely different path, by making attempts to re-direct their wealth in alternative sectors, such as manufacturing and construction. The most revolutionary approach was implemented in Qatar, which has introduced transparent financial practices and a regulatory body.

In terms of corporate governance, national governments in the Gulf region have responded to the global tendency for disclosure and transparency. A vivid example comes from Oman, where the Capital Market Authority (CMA) has requested disclosure of finances for all companies on the Muscat Securities Market since 2002. Similar initiatives have been undertaken in Kuwait and UAE (Saif and Choucair, 2009). The countries from the Gulf region have responded to the global tendency for disclosure of the distribution

of resources, which started with the recession in the Western capitalist societies, because of grief accusations against the remuneration systems in large corporations.

In general, the measures undertaken by the national governments of the GCC states have not been effective and their impact on reforming the ineffective and monolithic corporate sector in these countries has been insignificant. The global recession has sharpened already existing problems, related to the distribution of stakes and shares in corporations from the Gulf States. Balance has remained tilted in favour of big families, and little protection is offered for the smaller stakeholders. Corporate distribution of resources and patterns of ownership in the Gulf States remained burning issues throughout the recession, and have often been pinpointed by experts as possible reasons for these countries᾽ inability to implement its economic recovery measures efficiently.

2.6.5 Agency Problems in the Gulf Region

In order to understand corporate governance in the Gulf Region, it is important to highlight the main problems related to agency. There is a complexity of socio-economic, as well as historical factors, which define the state of corporate relations in the Gulf region, and their impact on firm performance and economic growth.

The first factor is related to the role of the family in ownership patterns and the importance of national culture (Ramady, 2010; Mababaya, 2003; Naciri and Naciri, 2008). One of the distinctive features of Gulf societies is the clan, which is a determinant not only for social, but also for business and commercial relations. As the literature review has shown, most of the large businesses in the region are still owned by the influential and affluent families in the region, which allows for a very personalised model of corporate model, where transparency and accountability in the decision-making processes remain on the demand side.

When defining the problems of agency in the Gulf States, it is important to mention the role of national culture and Islam in particular (Ramady, 2010). Many of the managerial practices and laws in these countries are based on the Islamic law, the Shariah, which has become the norm for conducting business on regional and international level. This is

where another important point needs to be made. The Gulf economies are characterised by heavy government intervention in business affairs and regulation. The corporate organisations are heavily dependent on government funding and regulation, which contributes for the closed monolithic structure of the business environment. At the same time, corporate governance laws and systems in the region remain feeble and ineffective. Although legal base for corporate governance is not entirely absent, many authors mention problems related with enforcement and implementation of the existing laws (Weir, 2011; Sourial, 2004). There is rarely any separation of responsibilities, and the minor shareholders have no voice in nominating directors. Also, they have hardly any role in the decision-making process, because of the authoritarian type of ownership and the role of the families, which have already been mentioned. "Boardroom passivity" is a common phenomenon in the corporations from the Gulf Region, and directors are poorly informed on company matters (Baydoun, Ryan and Willet, 2013). Also, in many Gulf countries there is a widespread shortage of independent non-executive directors, as well as external auditors.

Now unto the specific agency problems of the Gulf region, the Gulf Research Centre (2011) identifies three major problems with economic and financial agencies of the region as far as corporate governance is concerned. In the first place, there is the problem of uneven political, social and security interests among member countries. Even though the Gulf Research Centre (2011) notes that "the region's common economic interests were clearly outlined in the 1981 Unified Economic Agreement," there does not exist corresponding political, social and security interests among member states in the GCC and so most individual states carry out political, social and security agenda that indirectly affects the achievement of the set economic goals of various agencies. For instance it is common knowledge that the economic goals of the corporation cannot be attained at the agency level if there are outbreaks of political unrest as witnessed recently in the region. The same argument holds for social and security disparity. For this reason, until there will be corresponding political, social and security interests that match the economic interest of agencies the region would hardly have its total goals achieved.

Secondly, there is research centre mentions absence of monitoring regulations among agencies that ensure that member states benefit from the immense external investment that the region has been experiencing of late. For instance it is established that "according

to the 2008 World Economic Forum's Competitiveness Report, the small GCC states are the most competitive in the Middle East." However, there have not been any collective monitoring regulations among agencies to ensure that member countries benefit from revenue proceeds from investing companies. For this reason, companies keep showing up in the region and leave with huge accumulation of wealth without a corresponding benefit for member countries. This is contrary to other parts of the world such as the United Kingdom where there are rigid systems that ensure that investing companies and individuals pay as much as 50% tax to the state. Finally, there is an agency problem of lack of focus. This is a very serious problem that is worse felt when agencies are expected to show commitments to the GCC but are not able to do so because their individual member countries belong to other groups and organisations in the sub-region. Due to such varying associations, it has always been difficult for GCC agencies members to show a sense of focus and direction.

To conclude, other problems related to agency in the Gulf region are the low levels of transparency and accountability, which are to a large extent defined by the closed political system of these states and the absence of civil society and a dialogue between the public and the state. The uneven distribution of political and economic power in the Gulf countries is related not only to their political systems, but also to other factors such as low levels of literacy among the population and almost absent media publicity in terms of government/corporate decision-making.

2.7   Culture, Religion and Corporate Governance

Elements of honesty and trust play a crucial role in increasing the effectiveness of corporate governance framework (OECD, 2004). Cultural as well as religious characteristics of societies influence these values of honesty and trust and therefore, it can be said that culture and religion influence the governance practices also. Corporate governance plays a significant role in establishing a healthy relationship between board of directors, managers, shareholders and other stakeholders. A thorough understanding of the influence of culture becomes important in view of the fact the quality of corporate governance depends largely on the effective interaction among all the parties (Cheung and Chan, 2007). Since culture helps in the process of establishing a productive

negotiation among different actors involved in corporate governance-related issues, the relationship between the two elements has been researched extensively (Chan and Cheung, 2008). According to Licht (2001), the choice of corporate governance structure is changed on the basis of culture which shapes the interpersonal relationship of individuals and institutions. Culture also influences the values held by the decision makers which in turn impacts the changes in the organisational policies. Breuer and Salzman (2009) argue that culture plays an important role in deciding on the investors' objectives as well as ownership structure and therefore culture becomes responsible for the differences in corporate governance practices across countries. The relationship between cultural dimensions suggested by Hofstede and governance systems of corporate control and protection of minority shareholders is significantly explained by De Jong and Semenov (2006). The structure of corporate boards can be explained using Hofstede cultural model (Li and Harrison, 2008). Hofstede (1980) has developed a cultural model which consists of four different dimensions of organisational culture. According to Hofstede culture represents a collective social programme that can be used to define the set of values, beliefs, principles and attitudes that are shared by the constituents of a specific social community. Hofstede's approach to culture can be fitted into a corporate board considering it as a social community. It is argued that the national cultural dimensions of power distance, uncertainty avoidance, individualism/collectivism and masculinity/femininity identified by Hofstede could have a significant impact on the size, structure and leadership qualities of the members of a corporate board (Li and Harrison, 2008). For example, firms practising high level of uncertainty avoidance cultures normally tend to separate the position of CEO and the Chairman of the board. Thus, the behaviour and attitudes of the board members can be analysed from a cultural perspective using Hofstede's cultural model.

Hasan (2012) observe that in addition to culture, religion is also a likely determinant of business and corporate practices. The evidence for religion to have an influence on corporate governance practices has been provided on the assumption of general grounds of belief (Gellis et al. 2002). Especially in the GCC countries which are predominantly Muslim counties, religion plays a significant role in deciding the governance practices as the issues involved in the governance mechanisms are concerned with the ways in which people ought to behave rather than how they may behave in relation to different governance practices. Since there is no distinction between religious and secular affairs

in Islam, ethical behaviour is encouraged automatically by the voluntary ethical restraints imposed by the social pressure exerted by the community (Baydoun and Willett, 2000). Accordingly, in GCC countries Islamic Shariah provides for the foundation of the codes of conduct as well as the governance practices which mostly reflect the cultural and religious characteristics of the region (Islam and Hussain, 2003). Islamic Shariah prevails upon the core values of honesty, integrity and trust as the basic elements in ensuring ethical behaviour which are also considered the central values of corporate governance in general (Gambling and Karim, 1991). Hasan (2012) compared the corporate governance system in the Western countries and the corporate governance system based on Islamic principles and emphasised the essential role of ethics in ensuring better corporate governance system. According to Islamic principles, the ethical component of an economic activity must provide justice, honest and fairness to all connected parties to ensure that they get their rights and dues.

Baydoun and Willett (2000) have postulated certain basic tenets about the form and content of financial information as part of corporate governance mechanism, especially in presenting Islamic financial statements. According to the theory suggested by Baydoun and Willett (2000), the ways in which some of the accounting measures are interpreted and information disclosed to the stakeholders are affected by the practice of Islamic religion as a cultural base. This theory thus suggests the basic criteria for institution of corporate governance mechanism by insisting on a full disclosure and thrusting a social responsibility on the corporations. This leads to change in the scope of corporate governance in the economies following Islamic religion as compared to the codes of governance followed in Western economies. Abu-Tapanjeh (2009) observes that the dimensions of corporate governance from an Islamic perspective have broader outreach. Therefore, the roles and responsibilities of corporations cannot be compartmentalised in which all the actions and obligations of the corporations be made to fall only under the jurisdiction of the Islamic laws. Whereas, the Islamic laws would serve as the basic guide to implement the corporate governance principles suited to the Islamic nations like GCC countries.

With the economic development that took place in GCC countries in the last decades, there has been increased investments and the demand from the investors to raise the corporate governance standards has also gone up (Joshi and Wakil, 2004; Hussain and

Mallin, 2002). In addition, the governments of Gulf countries encourage the increased role of the private sector in their economic development. This necessitates inviting more foreign investment which in turn calls for instituting sound governance practices (Al Yafi, 2005). The Islamic principles of 'Shurah' implying consultation and the five necessities of Islam – religion, life, property, intellect and family – appear to govern the governance practices in GCC countries. While the principle of Shurah encourages consultation at high levels of management within the corporations, the religious ethical framework shapes the corporate governance mechanisms that would protect the property of not only the shareholders but also that of other stakeholders (Al-Khalifah, 1994).

Corporate governance in the GCC countries is structured as a balancing act of two key elements. First is the faith-based approach which regulates the conduct of business in accordance with Islamic law. Second is the profit-motive which involves conduct of business transactions with the intention of maximising shareholders' wealth (Matoussi and Grassa, 2012). This is evident from the corporate governance norms of Islamic banks and financial institutions. There is a complicated governance system in practice in which the banks and financial institutions are governed by the board of directors and a Shariah Supervisory Board (SSB) which act as the two internal corporate governance mechanisms. While the board of directors has the responsibility of protecting the interest of the shareholders and maximise their wealth, the SSB acts to protect the customer and Islamic community (Dar and Presley, 2000). The shariah governance approach in the GCC countries generally takes two forms. One of the mechanisms operates through legal and supervisory requirements as being practiced in Bahrain, Kuwait, UAE and Qatar. The second is the self-regulatory method as being practiced in Saudi Arabia.

The fundamental objective behind linking corporate governance with Islamic Shariah principles in GCC countries is that Shariah recognises the basic principles of governance namely social justice and accountability (Farook and Lanis, 2005). Because of this linkage, it becomes imperative that the ethical expectations of the community are embedded in the values, objectives and policies of corporations operating in the region. Thus, corporate governance in the GCC region is derived from the structure of corporate governance as originally envisaged but depending largely on ethical codes of Shariah. Bhatti and Bhatti (2009) observe that the principle of protection of the rights of

stakeholders including shareholders, investors, creditors, employees and the society are well covered by the principle of property rights in Islam.

From the discussion it follows that the Islamic system of corporate governance underpins practising ethical norms of transparency in all business transactions entered into by the corporations. Corporate governance from an Islamic principles perspective determines three distinct dimensions of decision-making. First is the mutual discussion using a consultative process; second is to regard the decision makers as trustees who have been given the necessary powers to take decisions in the best interest of all concerned; third is to have an effective religious supervision over all the decisions so that all operations of the corporations conform to the requirements of Shariah. Thus, corporate governance following Shariah principles provides comprehensive practice guidelines that encompass the duties and practices of all the actors to ensure transparency and honesty.

2.8   Conclusion

This paper reviews the previous literature on corporate governance to provide theoretical support to the research undertaken in the following chapters and to identify the possible research gap in relation to GCC countries. At the outset, the review focused on the theoretical bases of corporate governance as they evolved over time. We found that agency theory, one of the earliest theories relating to corporate governance, postulates that the objective of following corporate governance practices is to align the interests of management and the shareholders to increase the organisational value. While this theory has received the support of several earlier researchers, it is also criticised on the ground that it focuses only on the interest of the shareholders leaving aside the interests of other stakeholders. It is argued that such a stand may not be beneficial to the organisation in the long-run. Stakeholder theory proposed as an alternative to the agency theory is expected to consider the interests of all the stakeholders while using corporate governance mechanism to promote the organisational growth. However, stakeholder theory has also been considered to have shortcomings in that the conflicts of interests between different stakeholders may work against the organisational interest.

Subsequently we reviewed the two broad approaches – Anglo-Saxon approach and a multi stakeholder approach or combined approach – to corporate governance practices around the world. The Anglo-Saxon approach, practiced in countries like UK, US, Canada and Australia, is found to be closely related to agency theory focusing on the protection of the interests of the shareholders in preference to others'. This approach relies on free market operations as the correction mechanism providing a strong incentive to companies to minimise the agency costs to ensure survival and growth. Alternatively the combined approach practiced in most of the European countries takes its root in the stakeholder theory with the corporate governance practices to monitor the performance of the organisations from the perspectives of different stakeholders. As a part of the review we also looked at Japanese model, French and German models which are variations from the combined approach.

We then review the literature looking at the state and progress of corporate governance practices in the emerging markets. We find that privatisation and ownership patterns are the two major factors that have worked to shape the development of corporate governance practices in most of the emerging markets. Especially in the case of GCC countries, this finding provides the necessary theoretical support to the premise that the ownership pattern of companies has been the major factor in designing and implementing corporate governance practices. Family ownership of large companies in these countries has always influenced the design of corporate governance practices in the region.

We find that factors like extensive family ownerships, business group structures, and weak legal protection of minority shareholders have large influence on the shaping of corporate governance practices in the emerging markets including GCC region. The literature points out the existence of a strong relationship between better operating performance and market valuation with better corporate governance practices. Our review of the previous studies also highlights that the relative strength of legal systems and environments in different jurisdictions play a significant role in shaping the corporate governance practices. This finding is critical for our research because of the presence of legal systems in the Gulf economies possessing unique characteristics different from other emerging as well as developed economies. We argue that presence of weak system of corporate laws might influence the effectiveness of corporate governance practices in the GCC countries.

Our review of the previous literature also extended to the history of corporate governance in the Gulf region. We find that the development of corporate governance mechanism in the Gulf region is of recent origin. Since owners of large family-owned organisations in the region did not have the required technical knowledge to run their companies, they had to rely mostly on the professional managers appointed by them which in turn led to the separation of ownership and control. Earlier studies also indicate a slow progress of corporate governance practices in the region. However, the increased flow of foreign capital through institutional investors into the region during recent years has in fact presented a strong reason for the development of appropriate corporate governance mechanism in the region. The weak and under-developed capital markets in many of the GCC countries is found to be another reason for the slow progress in the development of corporate governance practices. Our review covered the development of corporate governance practices in Saudi Arabia including the creation of Capital Market Authority (CMA) and the promulgation of Capital Market Law which were found as the cornerstone of the development of corporate governance practices in the Kingdom of Saudi Arabia. Despite such development, the cultural and religious aspects specific to the GCC region have acted as a barrier to the development of sound corporate governance practices. One of the suggestions that evolved from the previous research studies is the need to develop a uniform system of corporate governance for all the member of countries of GCC as all these countries share common religious and cultural beliefs and their economic conditions are also more or less similar.

In addition to focusing on different elements influencing the effectiveness of corporate governance measures, the review embarked upon assessing the role of culture and religion on corporate governance. From the review, it emerge that culture has a prominent role in the design and implementation of corporate governance measures since culture influences the process of establishing a productive negotiation among multiple actors involved in governing the corporate institutions. Similarly, since religious characteristics of societies influence the values of honesty and trust, religion also plays an equally important role in determining the corporate governance initiatives within a country.

The literature review also covered the challenges in the development of a refined system of corporate governance practices in the GCC region. We find that the major challenge

for the implementation of corporate governance practices is the lack of stringent punishments or fines for not adhering to the corporate governance practices. The absence of punishments dilutes the purpose of the regulations imposed by various Gulf state governments. Our research also finds that the corporate governance standards prevailing in the GCC region are not comparable to global standards although the standards provide ample scope for the companies operating in the region to add value to the companies. We also observe that the corporate governance practices of GCC economies are drawn mostly from the Anglo-Saxon standards and hence they do not comply with the cultural and societal values of the region. Our review points out, despite the challenges, there is a large scope for the development and implementation of globally comparable corporate governance practices in the GCC countries.

Chapter 3.   Ownership Structure and Firm Performance in Gulf Corporation Council (GCC) Countries

Abstract

This paper investigates the impact of ownership structure on firm performance in Gulf Corporation Council (GCC) countries by examining 305 non-financial listed firms between 2006 and 2011. The study uses panel data fixed effect estimation techniques to analyse the impact of ownership on firm performance, measured with Tobin's Q and ROA. The findings based on Tobin's Q show that higher insider ownership leads to better performance, especially when insider owner is the Chairman. A larger ownership by institutional investors has a positive impact on firm performance. On the other hand, we find that GCC firms with high family ownership perform worse. We find that government ownership is negatively associated with performance when ROA is used as the performance measure.

3.1 Introduction

Corporate governance is a mechanism employed by providers of capital to corporations to ensure themselves that they will get a good enough return on their investment (Shleifer and Vishny 1997). The relationship between ownership structure and firm performance is important in shaping the corporate governance framework of a firm (Jensen and Meckling, 1976). The issue as to whether ownership structure matters for the performance of firms has been an important subject of debate in the finance literature. The empirical evidence on the impact of ownership structure on firm performance is mixed and sometimes contradictory. Some studies find that there is no significant relationship between ownership structure and firm performance. For example, Loderer and Martin (1997) find no evidence between managerial ownership and firm performance. Agrawal and Knoeber (1996) and Firth et al. (2002) provide evidence that ownership structure has no significant effect on firm performance based on a study of US and Chinese firms.

However, a large number of studies have shown that ownership structure affects performance. It is argued that ownership structures that affect performance negatively are ownership concentration (Johnson et al., 2000; Gugler and Weigand, 2003; Grosfeld, 2006; Holmstrom and Tirole, 1993), government ownership (Xu and Wang, 1999; Sun and Tong, 2003), family ownership (DeAngelo and DeAngelo, 2000; Fan and Wong, 2002; Schulze et al., 2001; Demsetz, 1983; Fama and Jensen, 1983; Shleifer and Vishny, 1997) and managerial ownership (Demsetz and Lehn, 1985).   On the other hand, structures with positive impact on the firm performance are foreign ownership (Arnold and Javorcik, 2005; Petkova, 2008; Girma, 2005; Girma and Georg, 2006; Girma et al., 2007; Chari et al., 2011; Mattes, 2008), managerial ownership (Jensen and Meckling, 1976; Chen et al., 2005; Drobetz et al., 2005)[4], institutional ownership (McConnell and Servaes, 1990; Han and Suk, 1998; Tsai and Gu, 2007), family ownership (Anderson and Reeb, 2003; Villanonga and Amit, 2006); Maury, 2006; Barontini and Caprio, 2006; Pindado et al., 2008) and government ownership (Sun et al., 2006).

This paper aims to examine whether ownership structure has an impact on firm performance in Gulf Corporation Council (GCC) countries. This is an important question

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[4] Furthermore, some studies suggest that there is no link between insider ownership and performance (e.g., Davies et al., 2005; Himmelberg et al., 1999).

as the region has witnessed significant economic growth over the last few decades. On the other hand, corporate governance practices are newly developing in the area and it is argued that lack of corporate governance is resulting in poor firm performance (Gellis et al., 2002; Islam and Hussain, 2003).

Several global economic developments make this research worthwhile to undertake. Firstly, GCC countries remain as major global economic players as oil producers. Regions' oil reserves accounts for over 40% of total global oil reserves. Due to increasing global oil demand GCC countries' has witnessed a tremendous increase in trade volume over the recent decade and this development has integrated these countries more to the global economy. Significant investments, including oil exploration and development of new oil fields, have been made by the GCC countries to establish themselves as a regional trade hub. Additionally, there are ongoing negotiations to establish free trade agreements with other regions and countries (such as the EU) and these factors will contribute positively to the region's integration into the global economy. GCC countries are currently working towards diversifying their economies from the oil sector into other sectors. Diversification is expected to increase trade among GCC member countries as well as with other countries (Sturm et al., 2008).

Secondly, despite its future economic prospects, it is argued that the GCC countries suffer from corporate governance issues (Musa, 2002). The development of corporate governance in the region and the governing rules has largely been largely influenced by religion, i.e. Islamic Sharia law (Gellis et al., 2002), which reflects the cultural and religious characteristic of the region (Islam and Hussain, 2003)[5].

Previous studies have argued that most businesses are controlled by a few shareholders and family ownership as well as state ownership is prevalent in the management of companies (Saidi, 2004; Union of Arab Banks, 2003). In addition, corporate boards are dominated by controlling shareholders, their relatives and friends and there is no separation of ownership which is often observed in developed countries. The number of

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[5] Islamic Sharia specifies a number of core values such as trust, integrity, honesty and justice which are similar to the core values of corporate governance codes in the West. However, a survey of corporate governance in a number of Gulf countries such as Saudi Arabia suggests that the region continues to suffer from corporate governance weaknesses. In addition, controlling shareholders tend to exhibit a lot of power over non-controlling shareholders and there is often insufficient disclosure of related party transactions (OECD, 2011).

independent directors in the boards is limited and the functions of the CEO and Chairman are carried out by the same person. The high concentration in firm ownership therefore undermines the principles of good corporate governance that are prevalent in western settings (Yasin and Shehab, 2004; World Bank, 2003; FRC, 2012).

Thirdly, there is a dearth of literature on the impact of ownership structure on firm performance in GCC countries. Rare examples are Arouri et al. (2014), who find that bank performance is affected by family ownership, foreign ownership and institutional ownership and that there is no significant impact of government ownership on bank performance and Zeitun and Al-Kawari (2012) who observe a significant positive impact of government ownership on firm performance.

Here we are motivated by the mixed results obtained in previous studies and the limited number of studies that have focused on GCC countries. The objective of the study is to explore in more details the factors that motivate particular types of ownership structure and the potential impact of ownership structure and firm performance in the Gulf region.

The remainder of the study is organised as follows. Section 3.2 provides a review of the literature on the relationship between ownership structure and firm performance. The literature review is divided into two subsections. The first subsection presents a theoretical framework on the relationship between ownership structure and performance and the second subsection presents a review of the empirical evidence on the link between ownership structure and firm performance. Section 3.3 presents a discussion of the methodology and a description of the data used in the study. Section 3.4 presents the empirical results and analysis. Finally, section 3.5 presents the conclusions.

3.2   Literature Review

In this section we provide a review of the literature on the link between firm performance and ownership structure. In two subsections we, firstly, look at the theories related to ownership structure and firm performance, and subsequently, review the empirical literature on the evidence.

3.2.1   Theoretical Framework

3.2.1.1 Transaction Cost Theory

Agency theory has been widely used as the basis for studying the relationship between ownership structure and performance. However, agency theory has been found to be inconclusive (Saravia and Chen, 2008). Consequently, there has been a shift in focus to transaction cost theory (TCT). The objective of TCT is to determine the governance mechanisms of various exchange transactions so as to maximise the economies for a given organisation (Williamson, 1991). It provides a basis for understanding corporate governance because it provides researchers with a more robust framework for analysing contracting issues that often occur between shareholders and managers (Saravia and Chen, 2008). Empirical evidence suggests that TCT can help in the analysis of corporate governance and corporate finance issues (Williamson, 1988; 1996). TCT comprises of three key dimensions as asset specificity, uncertainty, and frequency. Asset specificity is regarded as the most important dimension although the other two dimensions also play critical roles (Williamson, 1991).

Asset specificity can be described as the degree to which the cost of a transaction relationship is recoverable and used in another relationship (Ruzzier, 2009). High asset specificity results in risk in contract because the party with higher bargaining power could try to renegotiate the contract by threat of cancellation. In addition, during the transaction process, bounded rationality and information asymmetry can result in incomplete contracts because not all contingencies can be predicted in advance. Under such circumstances, transactions might not take place unless there is a guarantee that they will

yield high rents (Ruzzier, 2009). In order to overcome this dilemma, governance mechanism needs to be put in place to ensure that transactions are taking place at arm's length. The governance mechanism in place and thus influence the ownership structure of the firm, which can in turn influence the performance of the firm (Brian, 2010).

TCT has an effect on the ownership structure that a firm adopts and this implies that it can be used to explain the performance on firms. TCT can influence the ownership structure, which can in turn have an effect on the ownership structure (Brian, 2010). Williamson (1996) suggests that the analysis of corporate governance is concerned with the identification, explanation and mitigation of all forms of hazards and that firm and markets provide alternatives means to govern the firm.

3.2.1.2 Corporate Governance Theory

The principal-agent model is one of the major foundations of corporate governance theory. According to Williamson's (1963) "expense-preference" model, managers have two ways in which they can spend discretionary: i) emoluments and (ii) staff expenses. Emoluments include perquisite discretionary profits, which include expenses on staff expansion, physical plant, and equipment. Given that the principal (shareholder) aims at making profit while the agent (manager) aims at making emolument and discretionary profits, conflicts of interest exist between shareholders and managers. The maximisation of emoluments and profit would be aligned if more emoluments result in better management decisions. However, the management is likely to have a greater preference for emoluments and staff expenses, which mean that the utility maximisation of management preference may be in conflict with the profit maximisation preference of shareholders (Williamson, 1963). Utility maximising management will always incur more expenses on staff than on plant and equipment. This occurs because shareholders find it difficult to monitor the activities of managers. According to the economic principal-agent model, organisations can be regarded as nexus for contracts. According to Jensen and Meckling (1976), the principal-agent model can be considered as a relationship established by the principal with adequate incentives to motivate the agent to work in the best interest of the principal. However, given that the principal and the agent

have different interests and different access to information, the principal often finds it difficult to adequately monitor and evaluate the behaviour of the agent.

An economic principal-agent model is therefore about the ability of the principal to design compensation schemes that can motivate the agent to avoid indulging in opportunistic behaviour that will result in losses to the principal. Assuming rational expectations and self-interested behaviour, Barnea et al. (1981) provide a discussion of three roots of agency problems which include information asymmetry, debt financing, and partial ownership. Information asymmetry arises as a result of market imperfections. Accordingly, the agent tends to have more information than the principal. This information asymmetry makes it difficult for the principal to adequately monitor and evaluate the behaviour of the agent. With respect to information asymmetry, therefore, managers often take advantage of the fact that shareholders cannot adequately observe that behaviour and as such tend to maximise their personal interests rather than the interests of shareholders.

With respect to debt financing, equity shareholders have limited liability. As a result, equity holders are likely to undertake high risk projects which will result in the transfer of wealth from debtholders to shareholders if the projects are successful. However, the shareholder will just walk away because of limited liability if the projects are unsuccessful. Therefore, there are conflicts of interest between shareholders and debtholders. Shareholders use their advantage of limited liability to maximise their personal interest of profit maximisation while increasing the financial risk faced by debtholders (Myers 1977). Partial ownership occurs when the majority shareholders manage the business on a day-to-day business while minority shareholders have no control of the business. Under this circumstance, the majority shareholders may decide to pursue non-pecuniary benefits that may be in conflict with the interests of non-controlling or outside shareholders.

There are, therefore, two types of conflicts of interests including conflicts of interest between the principal and the agent arising as a result of information asymmetry and conflicts of interest between principals. The latter two roots of agency costs give rise to conflict of interests between principals. In the second case, the conflict of interest is between shareholders and debt-holders. This conflict of interest arises mainly because

shareholders enjoy limited liability. The debt-holder earns fixed interest on the principal amount that has been borrowed to the firm irrespective of the amount of profit that the firm makes. On the contrary, the shareholder's profit potential is unlimited. The shareholder is therefore motivated to take high risks that will enable him to make much profit. Taking such risk can cause the company to bankruptcy. In the event of bankruptcy, limited liability enables the shareholder to walk away from the firm leaving the debt-holder to incur all the losses that the firm has incurred. In the third case, one of the shareholder groups is in control of the organisation while the other group has no control over the organisation. In this case, the controlling shareholder group can undertake actions that are in line with maximising its private benefits at the expense of the non-controlling shareholder group. There are three main agency problems, which call for adequate corporate governance frameworks. These include adverse selection, hold-up and moral hazard.

Adverse selection is "an activity undertaken by a firm or individual that conveys information of a negative (or adverse) kind about their product or service" (Moles and Terry, 2012). Adverse selection is the result of information asymmetry (Black et al., 2013) and results in market failure which occurs as a result of difficulties in establishing contracts. Hold-up occurs when investors become concerned that future profits might be expropriated by managers. This leads to a reduction in the amount of investment investors are willing to make in the firm (Maher and Andersson, 1999). Moral hazard is a "situation in which a person or organisation has no incentive to act honestly or with due prudence" (Law, 2009). Jensen (2000) argues that different forms of corporate control influence firms. One of these forms is the ownership characteristic or structure. This internal control mechanism can influence the objectives of the firm, the level of discipline of managers and thus the value to shareholders.

Agency theory therefore contends that in firms with high ownership concentration, shareholders with control over the operations of the firm are likely to carry out activities that destroy the value of non-controlling shareholders (Francis et al., 2005; Miller et al., 2007; La Porta et al., 1999). Shareholders with control over the firm's operations are therefore more likely to maximise their personal interests in firms with a greater concentration of voting rights. Under such circumstances, ownership structure is expected to have a negative effect on the performance of the company. This trend may be

exacerbated in the case of family firms because those benefits remain in the controlling family, whereas in non-family firms, they are distributed among a large number of shareholders (Villanonga and Amit, 2006).

Agency problems exist between large and small shareholders in firms with high ownership concentration. Controlling and non-controlling shareholders also have conflicts of interests in firms with high ownership concentration (Francis et al., 2005; La Porta et al., 1999; Miller et al., 2007). When large shareholders control firms, their policies may lead to the expropriation of non-controlling shareholders. The conflict of interest between large and small shareholders can be numerous, including controlling shareholders enriching themselves by not paying out dividends or embarking on other expropriatory practices. Fan et al. (1999) provide evidence that ownership concentration and market valuation have a negative relationship.

Next we are focusing on empirical studies of the impact of ownership structure on firm performance and how different types of ownership affect firm performance across different countries.

3.2.2 Ownership Structures and Firm Performance

3.2.2.1 Concentrated Ownership

Concentrated ownership structure is an ownership structure in which a person or large block of shareholders (the controlling shareholder) holds an effective majority of the voting and equity rights of the corporation (Clifford, 2009). Unlike diversified minority shareholders, large block shareholders can shoulder the costs of being largely diversified and illiquid (Clifford, 2006). In corporations, large block shareholders are usually institutional investors such as mutual funds, pension funds and hedge funds. As ownership concentration increases, the monitoring power of investors increases. This is because these owners have incentives to proactively safeguard their investment. Large block shareholders can take aggressive actions over the firm decisions. Consequently,

concentrated ownership can be used as an internal governance mechanism that can be used to minimise the level of managerial opportunism (Grossfield, 2006).

Concentrated ownership is expected to have a positive impact on firm performance owning to the increased monitoring that it provides (Grosfeld, 2006). For example, Kapopoulos and Lazaretou (2006) provide evidence based on a simultaneous equation model for 175 listed firms in 2000 that a more concentrated ownership structure has a positive effect on firm performance. This indicates that a higher ownership concentration leads to more effective monitoring of the behaviour of management which in turn improves firm performance.

Dispersed ownership has been found to be less frequent than expected. Empirical evidence suggests that most firms are characterised by various forms of ownership concentration (La Porta et al., 1999). Given this high level of ownership concentration, there has been an increasing concern over the protection of the rights of non-controlling shareholders (Johnson et al., 2000; Gugler and Weigand, 2003). Empirical evidence shows that ownership concentration at best results in poor performance. Concentrated ownership is costly and has the potential of promoting the exploitation of non-controlling shareholders by controlling shareholders (Grosfeld, 2006). Holmstrom and Tirole (1993) argue that concentrated ownership can contribute to poor liquidity, which can in turn negatively affect performance. In addition, high ownership concentration limits the ability of the firm to diversify (Demsetz and Lehn, 1985; Admati et al., 1994).

3.2.2.2 Government Ownership

The impact of government ownership on firm performance has attracted the attention of many researchers because the government accounts for the largest proportion of shares of listed companies in some countries and also because government ownership can be used as an instrument of intervention by the government (Kang and Kim, 2012). Shleifer and Vishny (1997) suggest that government ownership can contribute to poor firm performance because Government owned enterprises often face political pressure for excessive employment. In addition, it is often difficult to monitor managers of government owned enterprises and there is often a lack of interest in carrying out business

process reengineering (Shleifer and Vishny, 1996; Kang and Kim, 2012). Contrary to Shleifer and Vishny (1997) some economists have argued that government ownership can improve firm performance in less developed and emerging economies in particular. This is because government ownership can facilitate the resolution of issues with respect to ambiguous property rights (Jefferson, 1998; Stiglitz 1996; Sun et al., 2002).

The empirical evidence on the impact of state ownership on firm performance is mixed. For example, Xu and Wang (1999) provide evidence of a negative relationship between state ownership and firm performance based on data for Chinese listed firms over the period 1993-1995. The study, however, fails to find any link between the market-to-book ratio and state ownership. Sun and Tong (2003) employ ownership data from 1994 to 2000 and compares legal person ownership with government ownership. The study provides evidence that government ownership negatively affects firm performance while legal person ownership positively affects firm performance. This conclusion is based on the market-to-book ratio as the measure of firm performance. However, using return on sales or gross earnings as the measure of firm performance, the study provides evidence that government ownership has no effect on firm performance. Sun et al. (2002) provide contrary evidence from above. Using data over the period 1994-1997, Sun et al. (2002) provide evidence that both legal person ownership and government ownership had a positive effect on firm performance. They explain their results by suggesting that legal person ownership is another form of government ownership. The above studies treat the relationship between government ownership and firm performance as linear.

The above studies were conducted in response to high ownership of Chinese companies by the state. Government ownership has also been investigated for other countries. For example, Huang and Xiao (2012) provide evidence that government ownership has a negative net effect on performance in transition economies. La Porta et al. (2002) provide evidence across 92 countries that government ownership of banks contributes negatively to bank performance. The evidence is consistent with Dinc (2005) and Brown and Dinc (2005) who investigate government ownership of banks in the U.S.

3.2.2.3 Family Ownership

Family ownership is very common in firms that are not listed (Arosa et al., 2010). There is a difference between family ownership and other types of shareholders in that family owners tend to be more interested in the long-term survival of the firm than other types of shareholders. This is likely to be the case for GCC countries because of the poor development of the stock market. Most companies are owned by small families (of between 3-10 family members), and thus GCC financial markets remain relatively small and represent approximately 1% of global assets. This shows that GCC financial markets are currently behind their potential. Therefore, the region faces tough challenges in competing with developed markets in Europe and America (Kern, 2012).

Furthermore, family owners tend to be more concerned about the firm's reputation of the firm than other shareholders (Arosa et al., 2010). This is because damage to the firm's reputation can also result in damage the family's reputation. Many studies have investigated the relationship between family ownership and firm performance in developed countries. They provide evidence of a positive relationship between family ownership and firm performance (e.g. Anderson and Reeb, 2003; Villalonga and Amit, 2006; Maury, 2006; Barontini and Caprio, 2006; Pindado et al., 2008).

The positive relationship between family ownership and firm performance can be attributed to a number of factors. For example, Arosa et al. (2010) suggest that family firms' long-term goals indicate that this category of firms desire investing over long horizons than other shareholders. In addition, because there is a significant relationship between the wealth of the family and the value of the family firm, family owners tend to have greater incentives to monitor managers (agents) than other shareholders (Anderson and Reeb, 2003). Furthermore, family owners would be more interested in offering incentives to managers that will make them loyal to the firm (Weber et al., 2003).

Additionally, there is a substantial long-term presence of families in family firms with strong intentions to preserve the name of the family. These family members are therefore more likely to forego short-term financial rewards so as to enable future generations take over the business and protect the family's reputation (Wang, 2006). Family ownership also has positive economic consequences on the business. There are strong control

structures that can motivate family members to communicate effectively with other shareholders and creditors using higher quality financial reporting with the resulting effect being a reduction in the cost of financing the business (Anderson et al., 2003). Furthermore, families are interested in the long-term survival of the firm and family, which reduces the opportunistic behaviour of family members with regard to the distribution of earnings and allocation of management positions (Anderson and Reeb, 2003; Panunzi and Shleifer, 2003).

Despite the positive impact of family ownership on firm performance, it has been argued that family ownership promotes high ownership concentration, which in turn creates corporate governance problems. In addition, high ownership concentration results in other types of costs (Arosa et al., 2010). As earlier mentioned, La Porta et al. (1999) and Vollalonga and Amit (2006) argue that controlling shareholders are likely to undertake activities that will give them gain unfair advantage over non-controlling shareholders. For example, family firms may be unwilling to pay dividends (DeAngelo and DeAngelo, 2000; Fan and Wong, 2002).

Another reason why family ownership can have a negative impact on firm performance is that controlling family shareholders can easily favour their own interests at the expense of non-controlling shareholders by running the company as a family employment service. Under such circumstances, management positions will be limited to family members and extraordinary dividends will be paid to family shareholders (Demsetz, 1983; Fama and Jensen, 1983; Shleifer and Vishny, 1997). Agency costs may arise because of dividend payments and management entrenchment (DeAngelo and DeAngelo, 2000; Francis et al., 2005). Families may also have their own interests and concerns that may not be in line with the concerns and interests of other investor groups (Shleifer and Vishny, 1997).

Schulze et al. (2001) provide a discussion, which suggests that the impact of family ownership on firm performance can be a function of the generation. For example, noting that agency costs often arise as a result of the separation of ownership from control, they argue that first generation family firms tend to have limited agency problems because the management and supervision decisions are made by the same individual. As such agency costs are reduced because the separation of ownership and control has been completely eliminated. Given that there is no separation of ownership and control in the first

generation family firm, the firm relationship between family ownership and performance is likely to be positive (Miller and Le-Breton-Miller, 2006). As the firm enters second and third generations, the family property becomes shared by an increasingly large number of family members with diverse interests. Conflict of interest sets in and consequently the relationship between family ownership and performance begins turning negative (Chrisman et al., 2005; Sharma et al., 2007). Furthermore, agency problems arise from family relations because family members with control over the firm's resources are more likely to be generous to their children and other relatives (Schulze et al., 2001).

3.2.2.4 Institutional Ownership

Institutional ownership can be regarded as the situation where most of the shares of a firm are owned by another institution. Institutional ownership has gained increased importance in equity markets and has also attracted a lot of attention from researchers. Empirical evidence suggests that institutional ownership has a positive impact on firm performance (e.g. McConnell and Servaes, 1990; Han and Suk, 1998; Tsai and Gu, 2007).

This positive impact has been attributed to the active monitoring argument. Accordingly, institutional investors have better monitoring techniques than retail investors. Institutional investors are more sophisticated, more professional and better informed than retail investors with respect to the functioning of capital markets, businesses, and industries. In addition, institutional investors higher capabilities in taking steps to monitor managers in a more effective and cost efficient manner (Hand, 1990).

Hartzell and Starks (2003) provide evidence of a negative relationship between managerial compensation and institutional ownership because institutional investors can replace incentive schemes aimed at aligning 'managerial interests with shareholder interests' with better monitoring. This ensures that agency problems are mitigated. The findings of Hartzell and Starks (2003) are consistent with earlier evidence provided in Pound (1988) and Hand (1990).

These findings have also been attributed to the 'institutional myopia argument', which suggests that institutional owners favour the achievement of short-term performance

targets and as such will use their influence to ensure that managers work towards meeting those targets. This in effect indicates that institutional ownership might not necessarily result in long-term positive performance since managers may not be encouraged to pursue projects that can contribute to the long-term success of the business. This argument is supported by the study by Wahal (1996) who provide evidence that the positive impact of institutional ownership on performance occurs only over short horizons. When longer horizons are taken into account, the impact of institutional ownership appears to be negative.

Another argument for the myopic behaviour of institutional investors is that institutional investors tend to be influenced by news regarding current earnings. Given that institutional investors regard the investment in a firm as an investment in one security in their portfolio, institutional investors tend to measure performance over short horizons (Porter, 1992; Coffee, 1991; Badrinath et al., 1989). A "strategic-alignment-conflict-of-interest" argument has also been suggested which suggests that institutional owners tend to focus on providing support to managers rather than monitoring and controlling their behaviour. This creates an interpersonal business relationship with the managers and benefits, which are higher than the gain that can be derived from effective monitoring. This accounts for the positive though short-term impact of institutional ownership on firm performance (Badrinath et al., 1989).

3.2.2.5 Foreign Ownership

Firms are increasingly owned by foreign companies owing to the recent surge in foreign direct investment (FDI). It is therefore important to look at how foreign ownership can influence firm performance. A few studies have taken this dimension. For example, Arnold and Javorcik (2005) argue that foreign ownership has a positive impact on firm performance in Indonesia. Petkova (2008) provides similar conclusions based on an analysis of plant level data in India. UK studies by Girma (2005), Girma and Georg (2006), and Girma et al. (2007) provide similar evidence that foreign ownership contributed positively to firm performance.

Chari et al. (2011) employ firm-level financial data to evaluate the impact of ownership of U.S. firms by firms from emerging markets during the period 1980-2006. The study provides evidence that U.S. firms acquired by emerging market firms witnessed an improvement in profitability during the years following the acquisition. This evidence suggests that foreign ownership of U.S. firms by firms from emerging markets contribute positively to performance. Likewise, Mattes (2008) investigated the impact of foreign ownership of German multinational firms and found that foreign ownership has a positive impact on performance. This is because of increased investment while availing an opportunity to expand to other countries (Nigh and Woodward, 1998). SMEinfo (2014) found out that foreign stakeholders also add the value of the firm through suggesting unique ideas, which help increase the level of competitiveness.

3.2.2.6 Managerial Ownership

Managers can own a significant number of the shares of the firm, which enables managers to gain performance incentives. The first studies of the relationship between managerial/insider ownership and performance were conducted in the 1970s. During this period, managers where often offered the opportunity to own shares in the firm as a means of aligning their interests with those of shareholders. Jensen and Meckling (1976) for example observe that there is a positive relationship between insider ownership and firm performance. Their study is based on the principal-agent model. Jensen and Meckling (1976) attribute the positive relationship between insider ownership and firm performance to the fact that managerial ownership enables the interests of managers to be more aligned with those of shareholders. This results in a reduction of agency problems, which in turn improves performance. Han (2006) for example observes a non-linear and significant positive impact to insider ownership on the performance of Real Estate Investment trusts (REITs). This study is consistent with the trade-off that exists between incentive alignment and managerial entrenchment (Han, 2006). Gugler et al. (2008) employ an average Tobin's Q and a marginal Tobin's Q to show that insider ownership has a positive impact on firm performance in the US. The study provides evidence of a positive impact of insider ownership on firm performance using both marginal and average Tobin's Q as measures of firm performance. The above studies however, fail to take into account the extra cost incurred in incentivising managers by offering them shares in the company

(Arosa et al., 2010). The question still remains as to whether the cost incurred in offering shares to managers are lower than the agency costs incurred to monitor the behaviour of managers (DeAngelo and DeAngelo, 2006; Fan and Wong, 2002). Furthermore, the alignment of managerial and shareholder interests is used as an argument against ownership concentration. Controlling for firm fixed effects, Himmelberg et al. (1999) fail to find any significant relationship between insider ownership and firm performance for US firms. Similar evidence is presented in Davies et al. (2005) for UK firms, as well as Fernandez and Gomez (2002) for a sample of Spanish firms. Furthermore, Firth et al. (2002) and Agrawal and Knoeber (1996) fail to find a significant impact of managerial ownership on firm performance based on a complex system of simultaneous equations.

Lack of evidence of a relationship between insider ownership and firm performance has been attributed to natural selection (Demsetz and Lehn, 1985) and the neutralisation (Eckbo and Smith 1998; Himmelberg et al., 1999) arguments. The natural selection hypothesis or argument states that investors with irrational expectations will eventually be forced out of the market by those with rational expectations (Gross, 2007). According to the mutual neutralisation hypothesis or argument, while performance impacts of different incentives are relevant, they tend to cancel one another out (Gross, 2007). However, Chen et al. (2005) observe that insider ownership has a significant positive impact in Japan. Similarly, Drobetz et al. (2005) in a study of the impact of insider ownership on firm performance among Swiss firms provides evidence that there is a significant positive impact of insider ownership on firm performance.

In addition to above literature, insider ownership is also analysed from the perspective of dispersed ownership. Fama and Jensen (1983) who observe that dispersed ownership creates a hold-up problem whereby shareholders find it difficult to prevent managers from indulging in opportunistic behaviour even though such behaviour might be apparent. Morck et al. (1988) and Stulz (1988) refer to the hold-up problem as "managerial entrenchment", whereby managers are capable of undertaking negative net present value projects because of the low risk of sanctions or takeovers.

Morck et al. (1988) observe that there is a high level of managerial ownership, the incentive alignment impact is higher than the entrenchment effect. This results in a combined positive impact on performance. Hubbard and Palia (1996) and Short et al.

(2002) suggest insider ownership thresholds of between 5% and 25%. Some studies have shown that performance can also affect insider ownership. For example, Loderer and Martin (1997) assume that managerial ownership and Tobin's Q are endogenous in a simultaneous equations framework. Their analysis suggests that an increase in managerial ownership improves performance while performance negatively affects managerial ownership. Al Farooque et al. (2007) provide similar evidence by observing a reverse-causality between the Tobin's Q and board ownership in Bangladesh. The above evidence suggests that both performance and insider ownership are endogenously determined.

3.2.2.6.1 CEO duality and ownership

CEO duality refers to the situation when the CEO also holds the position of the chairman of the board. CEO duality has been common throughout the corporate world. The percentage of CEO duality in the corporate firms remained around 80 per cent in the 1980s and 1990s, but in 2003 this percentage dropped to 60 per cent (Chen et al., 2008). Based on this trend, it can be deduced that the ownership structure has been mainly governed by a single person, performing the role of CEO and Chairman simultaneously. However, Falye (2007) argues that the non-duality ownership structure, separating Chairman's role from CEO, has substantially increased from 3 per cent in 2001 to 32 per cent in 2004.

Both the CEO and the Chairman have different roles and responsibilities. Within the context of the agency theory, conflict of interests takes place when principals (shareholders) delegate their powers to their agents (managers) particularly in the light of different corporate objectives and risk management strategies (Braun and Sharma, 2007). They further elucidate that as inherent differences grow, so do the attached agency costs including bonding, monitoring and structuring costs incurred to mitigate the effects of self-interests. However, the ultimate cost of corporate policies and strategies, which are devised and implemented by the CEO, is borne by the shareholders when the Chairman look differently at the CEO- proposed corporate policies (John, 1993). In other words, in the presence of conflict of interests between the CEO and the Chairman, the financial performance of company would be directly affected. Even in family-led institutions, the difference that the CEO and the chairman retain is not uncommon. For example, Boyd (1995) elaborates that this kind of conflict is mainly managed by drawing a line between

their roles; the CEO is authorised to make management decision, whereas the decision control enables the board to ensure smooth running of corporate policies and strategies. Pérez-González (2006) observes that inherited control has a negative effect on firm performance. A potential reason for this could be that when a CEO or chairman inherits a business, they might not be willing to put in the effort that the founder was putting in because the heir is not aware of the challenges that the founder has encountered in the process of building the business.

3.2.3 Ownership Structure and Firm Performance in GCC Countries

The GCC region comprises of a number of emerging countries. The governments in this region are characterised by high levels of corruption and face corporate governance issues (Nowak, 2001). Ownership concentration is high because practices such as rights issues have enable influential shareholders and influential familities to subscribe to new shares during Initial public offerings (IPOs) (Musa, 2002). Unlike the UK that has a corporate governance code (FRC, 2012), the region is yet to have a comprehensive corporate governance code.

There is a dearth of literature on the impact of firm ownership structure on firm performance in GCC countries. For example, Arouri et al. (2014) examine the impact of ownership structure on firm performance in GCC countries. Using a data set of 58 listed banks during the year 2010, the study provides evidence that the bank performance is affected by family ownership, foreign ownership and institutional ownership. The study does not observe any significant impact of government ownership on bank performance. While this study provides insights onto the impact of ownership structure on firm performance, it is characterised by a number of shortcomings. Firstly, the study focuses solely on banks, which means that the results cannot be generalised to firms in other industries. Secondly, the study employs cross-sectional data and focuses on a single year. It fails to take into account the effect of time-series changes in ownership structure on firm performance. Another study that has considered the impact of ownership structure on firm performance in GCC countries is Zeitun and Al-Kawari (2012). The study focuses exclusively on the impact of government ownership on firm performance based on data for 191 firms over the period 1999 to 2006. The study provides evidence that government

ownership has a significant positive impact on firm performance in GCC countries. This study is limited in that it focuses solely on government ownership, thereby ignoring the effects of other forms of ownership, such as family ownership, dispersed ownership and insider ownership.

We are motivated to fill the gap in the knowledge by investigating how ownership structure affects performance in the GCC countries. This study contributes to the literature in a variety of ways. Firstly, the study extends the literature on ownership structure to the Gulf region. It is one of the few studies that are considering this region. The Gulf region plays an important role in the global market place. As a major producer of oil and gas products, it remains a very important global player. An understanding of the performance of firms in this region is essential to investors who are interested in including the Gulf region in their portfolios. Secondly, the study contributes to the literature in that it makes use of a more comprehensive data set comprising of firm-specific, macroeconomic and corporate governance variables.

3.2.4 Government Ownership and Family Ownership and Profit Maximisation

Ownership concentration is the proportion of the shares of a company owned by a number of major shareholders. Ownership structure is one of the key elements in corporate governance which plays an important role in the contributing to firm performance (Saleh et al. 2009). In contrast to corporations functioning in the Western countries, enterprises operating in GCC countries are characterised to have concentrated ownership and a large number of block shareholders who are subjected to different levels of risk aversion and resource possession (Chahine, 2007). The relationship between ownership structure and corporate performance has received increased focus in the financial literature (Jiang, 2004; Karaca and Eksi, 2012). Ownership structure, because of its key role in firm performance, provides comprehensive insights into enhancing the systems of corporate governance. In developing countries like those in the GCC region, the concentration of ownership is said to result in poor or weak corporate governance system. According to agency theory, ownership concentration is a critical element in good corporate governance (Siala et al. 2009). However, ownership concentration provides an

opportunity to ensure control over the shareholder and managers so that such control could prevent oppression of minority shareholders (La Porta et al. 1999).

Al-Hassan et al. (2010) observe that governments of GCC countries have large stakes of ownership in most of the enterprises and banks. From a theoretical perspective government ownership is considered harmful to firm performance because of the excessive focus on their political and social goals which may hinder the allocation process of resources and thereby lead to reduction in the value and efficiency of firms (Najid and Abdul Rahman, 2011). Secondly, governments acting as agents of citizens not being the real owners are most likely to delegate their monitoring function to politicians and bureaucrats. The politicians and bureaucrats because of absence of interest in ensuring efficient running of the organisations may not perform effectively in discharging their monitoring functions (Ab Razak et al. 2008). According to Saleh et al. (2009) the human capital performance may be affected because of the fact that governments may appoint inexperienced staff in order to achieve their political and social objectives.

The rigid and bureaucratic supervision of the government-owned enterprises is also cited as a reason for their less efficient performance (Chang and Singh, 1997). In addition, since there are no incentives for managers they might not be inclined to pursue efficiency and maximise wealth of the government companies. The managers' drive towards efficient performance may be lowered because of easy availability of cheap and guaranteed financing. Such easy access to financing often might lead to inefficient utilisation of resources, low threat of the managers losing their jobs or even bankruptcy in some cases (Christensen, 1998). Studies also point out that privatisation could lead to improved performance in government-owned companies and help in solving agency problems (Vickers and Yarrow, 1991).

Empirical studies have supported the fact that government-owned enterprises have not performed better than private enterprises (Ahuja and Majumdar, 1998; Dewenter and Malatesta, 2001). It was also reported that there has been a significant improvement in operating performance of state-owned enterprises of Spain after they were privatised (Farinos et al. 2007). Some of the studies have also reported better performance of government-owned companies in comparison with private enterprises. For example, Dewenter and Malatesta, (2001) argue that government companies could perform better

than private companies because of the possibility of close monitoring of the managers than that is possible in private companies having dispersed ownership. Mak and Li (2001) observe that weaker accountability for financial performance, easier access to financing and lack of exposure in controlling corporations may hinder adoption of strong governance measures by government companies. Alignment of the managers of government companies with the political and social agenda of government companies detract them from focusing on maximising the firm value. Governments have to always place the interest of its citizens in the front and this has the effect of preventing the government companies to concentrate on profit maximisation. In many instances, governments are placed under the obligation to provide adequate employment opportunities to the public and they use the government companies as one of the means of creating additional employment. These political and social motives of governments often act to reduce the focus on effective implementation of corporate governance. Lopez-de-Salines et al. (1997) observe that governments have to respond to different interest groups (e.g. trade unions) in their act of meeting the social agenda. This results in the unlikely event of the government and the bureaucrats to provide any incentive to exercise governance measures over the government organisations or to ensure that they perform effectively in the matter of implementation of corporate governance.

GCC companies are characterised by a unique feature of family ownership which has a significant role in corporate governance firms. Family ownership has severe shortcomings in the form of managerial entrenchment and agency issues that have an adverse effect on firm performance (Braun and Sharma, 2007). The preference of family owners will be mostly to preserve the capital of the firm by resorting to risk reduction. They might also try to derive benefits from the firm at the cost of minority shareholders and might also be averse to long-term capital investments in view of short-term gains (Saleh et al. 2009). Family-owned firms may be reluctant to acquire knowledge-based assets because of the conservative nature of the owners (Fernandez and Nieto, 2006). Since family firm owners tend to appoint their family members in important managerial positions, outsiders appointed as managers might face cognitive conflicts. Managers may find it difficult to maintain professional relationships with family members appointed in key managerial positions. Such appointments of family members are most likely result in the absence of professional and qualified employees which in turn might affect the overall performance of the firm (Chen and Hsu, 2009).

Most of the family-owned firms in GCC being reasonably young have started as trading firms and have expanded into a wide range of businesses. Even some of the businesses have gained international stature in the past twenty to thirty years. Factors specific to emerging markets and the cultural heritage of the region have helped the family businesses to become successful (Saddi et al. 2009). A combination of factors like limited competition, wide opportunities and privileged access to capital and effective business networks has also ensured the success of these firms. The family-owned firms in GCC have advantages like more concentrated control and respect for the rules in passing the controls. However, such firms also suffer from disadvantages like the focus of the owners to enter into new businesses instead of increasing the scale of existing businesses and institutionalising them. Another issue with family owners is their emotional attachment to businesses started earlier although returns from such businesses are below cost (Saddi et al. 2009). These qualities of family business specific to the GCC region in addition to the general problems discussed earlier make the implementation of corporate governance in family-owned firms of GCC countries a complex affair. Previous research using empirical studies on the impact of ownership structure on firm performance were unable to provide conclusive results (Turki & Sedrine, 2012; Fazalzadeh et al. 2011; Uwalomwa & Olamide, 2012). There appears to be a dearth of research studies that examined the relationship between different dimensions of ownership structures and their impact on firm performance in the context of Gulf countries.

3.3 Methodology

3.3.1 Empirical Model

We contribute to the above mentioned literature on the impact of ownership structure on firm performance in the GCC countries[6]. This study will make use of the Tobin's Q and return on assets (ROA) to measure firm performance. This is in line with earlier studies which employ the Tobin's Q and ROA as dependent variables (for example Morck et al., 1988; Loderer and Martin, 1997; McConnell and Servaes, 1990; Kapopoulos and Lazaretou, 2006; Chen et al., 2005; Al Farooque et al., 2007; and Demsetz and Lehn, 1985).

The Tobin's Q is the ratio of the market value of a firm to the replacement value of its assets. We calculate Tobin's Q as the ratio of the book value of total assets minus the book value of equity plus the market value of equity to the book value of assets. ROA measures the overall effectiveness of management in generating returns to ordinary shareholders. It is calculated as the ratio of net income to total assets.

Two major differences exist between the Tobin's Q and ROA. The first difference comes as a result of the time perspective. Accordingly, the Tobin's Q is a forward looking measure because it depends on how investors evaluate the firm's future performance. ROA on the contrary is a backward-looking measure of performance. A high Tobin's Q is an indication that investors have a positive perception of the firm's future performance based on their evaluations of the investments it has deployed. In other words, the market's valuation of the firm is higher than the accounting valuation. The second difference between the Tobin's Q and ROA can be attributed to accounting concerns. ROA is calculated from information obtained from the financial statements. The items reported

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[6] The philosophical context of the research design is Positivism. According to Salkind (2010), under Positivism doctrine, scientific process of human reasoning is the most suitable method of research design. The two main ingredients of Positivism are experience and transparency (Gartrell and Gartrell, 1996). The transparency is the extent to which the data can be verified. The application of empirical research design requires developing a robust empirical model. This empirical model will be responsible in measuring the relationship between variables under consideration in the research and a suitable set of historical data extracted from trusted sources. These are the two main pillars of empirical research design according to Sorenson (2002).

in financial statements are constrained by accounting standards and are subject to manipulation. ROA can thus be influenced by differences in accounting standards across countries, such as the different methods applied in the valuation of intangible and tangible assets in the balance sheet (Kapopoulos and Lazaretou, 2006).

Panel data is used to analyse the impact of ownership structure on firm performance. Panel data analysis is a regression approach that combines both time-series and cross-sectional data (Baltagi, 2005). Panel data enables a researcher to include variables that cannot be measured or observed such a differences in business practices across companies or differences in culture across countries. It also enables a researcher to analysis variables that change with time but not across firms. In general, panel data analysis controls for individual heterogeneity and often analysed using two techniques including fixed effects and random effects models (Baltagi, 2005; Torres-Reyna, 2007).

Fixed effects models are used when the research is only interested in analysing the effect of variables that vary with time (Torres-Reyna, 2007). Fixed effects models explore the relationship between the independent and dependent variables within a firm. Each firm has its own individual effects that may or may not affect the dependent variable. Fixed effects models assume that firm-specific effects can influence the independent variable. Consequently, fixed effects need to be controlled for. Fixed effects, therefore, eliminate the impact of time-invariant characteristics thus enabling the researcher to assess the net impact of the independent variables on the dependent variable (Torres-Reyna, 2007).

Unlike the fixed effects model, the random effects model assumes that the variation across firms is random and not correlated with the dependent or independent variables (Torres-Reyna, 2007). The major difference between random and fixed effects is whether the individual effects embody elements that are correlated with the independent variables in the model rather than whether the effects are stochastic or not (Baltagi, 2005; Torres-Reyna, 2007). Random effects models should therefore be used when the research believes that differences across entities have an impact on the dependent variables. Otherwise, the fixed effects model should be used.

In this study, we employ fixed effects regression models given the Hausman test results. The Hausman test is based on the difference between the fixed and random effects

estimators (Baltagi, 2005). A rejection of the null hypothesis in the Hausman test is an indication that the fixed effects should be used. As will be observed in the analysis section, the Hausman test was conducted for all the regressions and based on the results the fixed effect model was selected over the random effects model.

We employ independent variables that are divided into four groups as:

1. Ownership structure including managerial ownership, family ownership, government ownership, institutional ownership, foreign ownership and concentrated ownership. All ownership variables are more than or equal to 5% of the total ownership of any firm under study. This is because firms in GCC countries only report percentage of shares that is either greater than or equal to 5 percent.
2. Board characteristics including CEO duality, board size, executive directors and independent directors.
3. Financial characteristics including leverage and firm size.
4. Macroeconomic variables including GDP growth and year dummy variables.

The definitions for all the variables used in this study are presented in Table 3.1.

We estimate the following models to examine the relationship between ownership structure and firm performance in GCC countries. First we start with our baseline model (1) distinguishing between managerial and external ownership. This model is given below:

$$
\begin{aligned}
Performance_{i,t} = {} & \beta_0 + \beta_1 Managerial\ Ownership_{i,t} + \beta_2 External\ Ownership_{i,t} \\
& + \beta_3 Family\ Ownership_{i,t} + \beta_4 Board\ Size_{i,t} + \beta_5 Executive\ Directors_{i,t} \\
& + \beta_6 Independent\ Directors_{i,t} + \beta_7 Firm\ Size_{i,t} + \beta_8 Leverage_{i,t} \\
& + \beta_9 GDP\ Growth_{c,t} + \sum_{y=1}^{Y-1} \beta_y \times Year_{i,y} + e_{i,t,c,y}
\end{aligned}
$$

Table 3.1 Definitions of dependent and independent variables

This table reports the definition of the variables that are used in the study. For ownership variables we do not report the values if shares owned is less than 5 per cent. All the variables are measured at the end of each year. Sources: Thomson one.com, Datastream and annual reports of the companies.

Performance measures

Tobin's Q	The ratio of the book value of total assets minus the book value of equity plus the market value of equity to the book value of assets
Return on assets (ROA)	The ratio of net income to total assets

Board Characteristics

CEOChair	Equals 1 if CEO and chairman are different person, 0 if CEO and chairman are the same person
Board size	The total number of directors on the board
Executive directors	The number of executive directors divided by the board size
Independent directors	The number of independent directors divided by the board size

Ownership Structure

Managerial ownership	The percentage of shares owned by managerial (CEO and chairman) for shareholding of 5 per cent or more
CEO ownership	The percentage of shares owned by the CEO for shareholding of 5 per cent or more
CEO family	Equals to 1 if the CEO is a member of the family owning the company and 0 otherwise
CEO family ownership	The percentage of shares owned by CEO who is a member of the family owning the company for shareholding of 5 per cent or more
Chairman ownership	The percentage of shares owned by chairman for shareholding of 5 per cent or more
Chairman family	Equals to 1 if the chairman is a member of the family owning the company and 0 otherwise
Chairman family ownership	The percentage of shares owned by chairman who is a member of the family owning the company for shareholding of 5 per cent or more
Family ownership	The percentage of shares owned by family for shareholding of 5 per cent or more
Non-family ownership	The percentage of shares owned by non-family for shareholding of 5 per cent or more
External ownership	The percentage of shares owned by outsiders. It equals to total ownership minus the total of managerial and family ownership for shareholding of 5 per cent or more.
Institutional investor ownership	The percentage of shares owned by corporation, investment manager, investment funds and government for shareholding of 5 per cent or more
Domestic institutional ownership	The total number of institutional investors who are operating in the same country domestically
Foreign institutional ownership	The total number of foreign institutional investors
Non-governmental institutional ownership	The percentage of shares owned by corporations, investment managers and investment funds for shareholding of 5 per cent or more
Corporation ownership	The percentage of shares owned by corporations for shareholding of 5 per cent or more
Domestic corporation ownership	The total number of corporation owners who are operating in the same country domestically
Foreign corporation ownership	The total number of foreign corporation owners
Investment manager ownership	The percentage of shares owned by investment managers for shareholding of 5 per cent or more
Domestic investment manager ownership	The total number of investment manager owners who are operating in the same country domestically
Foreign investment manager ownership	The total number of foreign corporation owners
Individual investor ownership	The percentage of shares owned by individual investors for shareholding of 5 per cent or more
Government ownership	The percentage of shares owned by local government for shareholding of 5 per cent or more
Foreign ownership	The total numbers of foreign owners, whether they are institutional or individual
Concentrated ownership	The log of Herfindahl Index for measuring concentrated ownership. The Herfindahl index is defined as the sum of the squared sums of all owners shareholdings

Financial and economic characteristics

Leverage	The ratio of total debt to total liabilities
Firm size	The natural logarithm of total assets
GDP growth	The GDP growth rate of the economy which is the company is operating in
Year dummy variables	Each dummy variable equals to 1 for the specific year variables (2006 to 2011) are reported and 0 otherwise

In the first stage of our analysis, we separate managerial ownership as CEO ownership and Chairman Ownership in model (2) given below:

$$Performance_{i,t} = \beta_0 + \beta_{1A}CEO\ Ownership_{i,t} + \beta_{1B}Chairman\ Ownership_{i,t}$$

$$+ \beta_2External\ Ownership_{i,t} + \beta_3Family\ Ownership_{i,t} + \beta_4Board\ Size_{i,t}$$

$$+ \beta_5Executive\ Directors_{i,t} + \beta_6Independent\ Directors_{i,t}$$

$$+ \beta_7Firm\ Size_{i,t} + \beta_8Leverage_{i,t} + \beta_9GDP\ Growth_{c,t} + \sum_{y=1}^{Y-1} \beta_y \times Year_{i,y}$$

$$+ e_{i,t,c,y}$$

We then distinguish between family and non family CEO's and Chairman by interacting these variables with family ownership in models (3) and (4):

$$Performance_{i,t} = \beta_0 + \beta_{1A}CEO\ Ownership_{i,t} + \beta_{1C}CEO\ Family_{i,t}$$

$$+ \beta_{1D}CEO\ Family\ Ownership_{i,t} + \beta_{1B}Chairman\ Ownership_{i,t}$$

$$+ \beta_2External\ Ownership_{i,t} + \beta_3Family\ Ownership_{i,t}$$

$$+ \beta_4Board\ Size_{i,t} + \beta_5Executive\ Directors_{i,t}$$

$$+ \beta_6Independent\ Directorss_{i,t} + \beta_7Firm\ Size_{i,t} + \beta_8Leverage_{i,t}$$

$$+ \beta_9GDP\ Growth_{c,t} + \sum_{y=1}^{Y-1} \beta_y \times Year_{i,y} + e_{i,t,c,y}$$

$$Performance_{i,t} = \beta_0 + \beta_{1A}CEO\ Ownership_{i,t} + \beta_{1B}Chairman\ Ownership_{i,t}$$

$$+ \beta_{1E}Chairman\ Family_{i,t} + \beta_{1F}Chairman\ Family\ Ownership_{i,t}$$

$$+ \beta_2External\ Ownership_{i,t} + \beta_3Family\ Ownership_{i,t}$$

$$+ \beta_4Board\ Size_{i,t} + \beta_5Executive\ Directors_{i,t}$$

$$+ \beta_6Independent\ Directors_{i,t} + \beta_7Firm\ Size_{i,t} + \beta_8Leverage_{i,t}$$

$$+ \beta_9GDP\ Growth_{c,t} + \sum_{y=1}^{Y-1} \beta_y \times Year_{i,y} + e_{i,t,c,y}$$

In the second stage of our analysis we separate external ownship to its components; including institutional ownership and individual ownership as given below in model (5):

$$
\begin{aligned}
Performance_{i,t} = \ & \beta_0 + \beta_1 Managerial\ Ownership_{i,t} \\
& + \beta_{2A} Institutional\ Ownership_{i,t} + \beta_{2B} Individual\ Ownership_{i,t} \\
& + \beta_3 Family\ Ownership_{i,t} + \beta_4 Board\ Size_{i,t} \\
& + \beta_5 Executive\ Directors_{i,t} + \beta_6 Independent\ Directors_{i,t} \\
& + \beta_7 Firm\ Size_{i,t} + \beta_8 Leverage_{i,t} + \beta_9 GDP\ Growth_{c,t} + \sum_{y=1}^{Y-1} \beta_y \times Year_{i,y} \\
& + e_{i,t,c,y}
\end{aligned}
$$

Subsequently we distinguish between different types of institutional owners as: corporation, investment manager and government given in the model (6) below:

$$
\begin{aligned}
Performance_{i,t} = \ & \beta_0 + \beta_1 Managerial\ Ownership_{i,t} \\
& + \beta_{2C} Corporation\ Ownership_{i,t} \\
& + \beta_{2D} Investment\ Manager\ Ownership_{i,t} \\
& + \beta_{2E} Government\ Ownership_{i,t} + \beta_{2B} Individual\ Ownership_{i,t} \\
& + \beta_3 Family\ Ownership_{i,t} + \beta_4 Board\ Size_{i,t} \\
& + \beta_5 Executive\ Directors_{i,t} + \beta_6 Independent\ Directorss_{i,t} \\
& + \beta_7 Firm\ Size_{i,t} + \beta_8 Leverage_{i,t} + \beta_9 GDP\ Growth_{c,t} + \sum_{y=1}^{Y-1} \beta_y \times Year_{i,y} \\
& + e_{i,t,c,y}
\end{aligned}
$$

We also distinguish between foreign and domestic institutional ownership for each category and other combination of our main explanatory variables. These models are presented in the results tables but not shown here.

3.3.2 Data and Sources

The objective of the research design is to concentrate on the ownership structure of GCC countries' companies. Due to data availability our sample includes five countries from the GCC, which are Kuwait, Oman, Qatar, Saudi Arabia and United Arab Emirates. For example, Bahrain is characterised only by financial firms with no available data and, consequently not included in the study.

Our sample includes 305 listed firms for the period between 2006 and 2011. Financial firms such as banks and insurance companies were excluded from this study due to the unique nature of the sector and the inconsistency and variations in the calculations of Tobin's Q. Our sample holds 126 firms for Kuwait, 107 firms for Saudi Arabia, 82 firms for Oman, 25 firms for Qatar and 22 firms for the United Arab Emirates, for a total sample of 362. In different estimations some of the observations drop due to missing variables.

The data is gathered from different sources, namely, Thomson one banker, Thomson.com, Datastream and annual reports. All of the board characteristics data is manually collected from the annual reports of the firms. Financial data is obtained from Thomson One Banker and Datastream. Ownership structure data is obtained from Thomson.com.

3.3.3 Descriptive statistics

Table 3.2 presents the descriptive statistics of the variables included in the study. We begin by looking at the ownership variables. It can be observed that managerial ownership has a mean of 3.55 and a standard deviation of 10.27. Based on the relatively high standard deviation, one can say that managerial ownership varies considerably across entities and across time in the GCC countries.

Table 3.2 Descriptive statistics

This table reports descriptive statistics of the variables that are used in the study. For ownership variables we do not report the values if shares owned is less than 5 per cent. All the variables are measured at the end of each year. Sources: Thomson one.com, Datastream and annual reports of the companies. Definitions for all the variables are provided in Table 3.1.

Variable	Number of observations	Mean	Median	Std. Dev	Minimum	Maximum
Performance measures						
Tobin's Q	1074	1.87	1.18	1.78	0.14	12.90
Return on assets (ROA)	1074	6.81	6.67	10.10	-44.93	47.54
Board Characteristics						
CEOChair	1074	0.50	1.00	0.50	0.00	1.00
Board size	1074	7.17	7.00	1.89	3.00	13.00
Executive directors	1074	0.77	1.00	0.84	0.00	8.00
Independent directors	1074	5.47	5.00	2.16	0.00	12.00
Ownership Structure						
Managerial ownership	1074	3.55	0.00	10.27	0.00	95.00
CEO ownership	1074	0.49	0.00	2.62	0.00	23.20
CEO family	1074	0.10	0.00	0.31	0.00	1.00
CEO family ownership	1074	0.30	0.00	2.11	0.00	23.20
Chairman ownership	1074	3.06	0.00	9.81	0.00	95.00
Chairman family	1074	0.38	0.00	0.49	0.00	1.00
Chairman family ownership	1074	2.47	0.00	9.22	0.00	95.00
Family ownership	1074	5.70	0.00	15.26	0.00	99.25
Non-family ownership	1074	6.90	0.00	13.55	0.00	95.00
External ownership	1074	46.22	46.80	24.06	2.40	99.90
Institutional investor ownership	1074	35.48	33.24	26.60	0.00	99.90
Domestic institutional ownership	1074	1.50	1.00	1.24	0.00	7.00
Foreign institutional ownership	1074	0.30	0.00	0.50	0.00	2.00
Non-governmental institutional ownership	1074	29.33	23.55	25.94	0.00	99.90
Corporation ownership	1074	22.43	14.31	24.95	0.00	99.90
Domestic corporation ownership	1074	0.92	1.00	1.07	0.00	6.00
Foreign corporation ownership	1074	0.04	0.00	0.19	0.00	1.00
Investment manager ownership	1074	6.99	0.00	15.26	0.00	86.91
Domestic investment manager ownership	1074	0.33	0.00	0.72	0.00	6.00
Foreign investment manager ownership	1074	0.00	0.00	0.07	0.00	1.00
Individual investor ownership	1074	12.56	0.00	18.93	0.00	99.25
Government ownershiop	1074	6.33	0.00	14.75	0.00	81.20
Foreign ownership	1074	0.33	0.00	0.67	0.00	3.00
Concentrated ownership	1074	1221	564	1659	6	9980
Financial and economic characteristics						
Leverage	1074	0.23	0.18	0.21	0.00	2.00
Firm size	1074	5.35	5.31	1.79	0.54	11.39
GDP growth	1074	5.00	4.64	4.78	-5.15	18.80

The descriptive statistics indicates that in respect of managerial ownership the mean CEO own share is 0.49 and a standard deviation of 2.62. This proportion appears to be high as compared to developed countries where the mean value of managerial ownership is 0.0931 (Ruan et al. 2009). This also shows that there is high variability of CEO own share across time and entities in GCC countries.

In this study, similar results can be observed for other ownership structures like CEO family, CEO ownership family, Chairman own share, Chairmen family chair ownership family and family own. Non-family shows that these categories have a mean of 6.90 and a standard deviation of 13.55. This shows that there is also high variability across time and entities. External ownership has a mean of 46.22 and a standard deviation of 24.06. The standard deviation is quite low compared to the mean suggesting that the variability of individual observations of external ownership across time and entities is not very high. Institutional ownership has a mean of 35.48 and a standard deviation of 26.60. Similar evidence can be observed for Non-governmental institutional ownership. Foreign institutional ownership and domestic institutional ownership have very low means and standard deviations.

Corporation ownership has a mean of 22.43 and a standard deviation of 24.95 indicating the extent of variations in the distribution of variables. Individual investor ownership has a mean value of 12.56 and a standard deviation of 18.93 implying that there is some element of variation in the distribution of the concerned variables. In this study the descriptive study indicates that Government ownership has a mean of 6.33 and a standard deviation of 14.75. This finding shows that the variability of individual observations of government ownership is considerably high across time and firms. Overall, the concentrated ownership has a mean of 1221 and a standard deviation of 1659. This indicates that ownership concentration is high. The high standard deviation also shows that ownership concentration varies considerably across time and firms.

Looking at the performance measures, it can be observed that the mean Tobin's Q is 1.87 with a standard deviation of 1.78. The standard deviation and the mean do not differ significantly suggesting that individual observations do not vary considerably across time and firms. The mean Tobin's Q is also higher than 1.0 suggesting that most of the firms in the GCC region were selling at a premium to book value (Kapopoulos and Lazaretou,

2006). ROA has a mean of 6.81 and a standard deviation of 10.10 suggesting that ROA varies considerably across time and firms.

Looking at the Board characteristics, it can be observed that the CEO Chair had a mean of 0.50 and a standard deviation of 0.50. The board size had a mean value of 7.17 and a standard deviation of 1.89. Executive directors had a mean of 0.77 and a standard deviation of 0.84. The Independent Directors had a mean of 5.47 and a standard deviation of 2.16. It is worth noting that the region seems to be characterised by strong corporate governance rules. Based on the board characteristics of the sample companies, it appears that GCC companies have a large number of independent directors. This is evident from the higher mean value for independent directors in the Board than the number of executive directors. Moreover, the Board mean board size is somewhat high at 7.17 suggesting that the region has a strong corporate governance framework. Again the board size in the US companies has a higher mean value of 9.27 implying that the GCC companies need to improve their corporate governance performance by suitably modifying the board structure and composition (Chen et al., 2008).

3.3.3.1 Descriptive Statistics by Country

We present the mean values of the variables for each country in Table 3.3. As shown, United Arab Emirates had the lowest number of CEO Chairs while Saudi Arabia had the highest number of CEO Chair of boards. Qatar had the highest number of board members while Kuwait had the least number of members in the boards. Government shareholding was the highest in United Arab Emirates and the lowest in Qatar. The results show that United Arab Emirates has the highest family ownership of 13.20% while Qatar had none of the firms with family ownership recorded since the number could not meet the 5% threshold. Saudi Arabia had the highest chairman family ownership at 4.57% with United Arab Emirates recording the least ownership of 1.12%. Table 3.3 further shows that Tobin's Q was the highest in Kuwait and the lowest in United Arab Emirates. This suggests that generally, firms in Kuwait performed better than other firms in GCC countries. The results also show that GDP growth was the highest in Qatar and the lowest in Kuwait. This is expected as Qatar has had a very robust economic growth for years

now and therefore outperforms the rest of the GCC countries. Leverage was the highest in Oman and the lowest in United Arab

Table 3.3 Mean values of the variables by country

This table reports descriptive per country mean values of the variable used in the study. For ownership variables we do not report the values if shares owned is less than 5 per cent. All the variables are measured at the end of each year. Sources: Thomson one.com, Datastream and annual reports of the companies. Definitions for all the variables are provided in Table 3.1.

Variable	Qatar	United Arab Emirates	Kuwait	Oman	Saudi Arabia
Performance measures					
Tobin's Q	0.69	0.67	3.41	1.36	0.81
Return on assets (ROA)	7.73	6.70	6.85	7.54	5.99
Board Characteristics					
CEOChair	0.56	0.35	0.41	0.53	0.61
Board size	8.88	7.29	5.97	7.20	8.20
Executive directors	1.24	0.47	0.59	0.39	1.22
Independent directors	7.52	6.88	5.38	6.20	4.27
Ownership Structure					
Managerial ownership	1.41	1.36	2.47	1.59	7.89
CEO ownership	0.00	0.24	0.29	0.23	1.18
CEO family	0.12	0.06	0.14	0.02	0.13
CEO family ownership	0.00	0.00	0.29	0.00	0.70
Chairman ownership	1.41	1.12	2.18	1.36	6.71
Chairman family	0.48	0.56	0.40	0.42	0.27
Chairman family ownership	1.41	1.12	2.08	1.36	4.57
Family ownership	0.00	13.20	5.30	5.33	5.90
Non-family ownership	1.96	3.00	4.67	6.55	12.77
External ownership	43.94	44.08	47.73	50.89	40.70
Institutional investor ownership	41.99	33.67	40.85	39.85	22.03
Domestic institutional ownership	1.12	1.13	2.09	1.15	0.96
Foreign institutional ownership	0.06	0.38	0.23	0.38	0.37
Non-governmental institutional ownership	41.01	24.33	36.68	31.37	14.24
Corporation ownership	12.40	17.86	30.03	27.06	8.51
Domestic corporation ownership	0.35	0.57	1.43	0.72	0.41
Foreign corporation ownership	0.06	0.14	0.02	0.06	0.02
Investment manager ownership	28.61	6.47	6.65	4.73	5.74
Domestic investment manager ownership	0.76	0.33	0.45	0.11	0.21
Foreign investment manager ownership	0.00	0.00	0.00	0.00	0.02
Individual investor ownership	1.96	16.20	9.89	11.88	18.67
Government ownership	0.98	9.35	4.17	9.32	7.79
Foreign ownership	0.16	0.30	0.10	1.00	0.19
Concentrated ownership	2291	1276	994	1627	1075
Financial and economic characteristics					
Leverage	0.22	0.14	0.23	0.28	0.19
Firm size	6.61	5.88	5.45	3.75	6.15
GDP growth	16.95	3.52	3.50	5.94	3.52

Emirates. This suggests that firms in Oman were highly leveraged than any other firms among the GCC countries and could suggest the riskiness of firms in Oman.

3.3.3.2 Descriptive Statistics by Year

Table 3.4 presents the mean values for all the variables by year. As shown, board size averaged 7 members with the highest number recorded in 2009 and subsequent years, just after the global financial crisis. It is also interesting to note that family ownership has been dropping with the highest levels of 32.50% in 2006 to the lowest of 5.43% in 2011. During this period, most firms changed from private ownership to public ownership. The ownership by chairman of the companies has also been decreasing since 2006 when the ownership was 3.50% to 2.16% in 2011. One may attribute this factor to the decrease in control of chairpersons over the firms as cautioned by the effects of the 2008 financial crisis. They thus have to delegate most of their duties. Table 3.4 further shows that the GDP growth ranged from the low of -0.76 in 2009 to a high of 7.72 in 2011. The slump in economic performance of GCC countries in 2009 was the result of global financial crisis. The countries soon recovered and recorded the highest performance in 2011. The results also show that leverage was the highest in 2008 and the lowest in 2006 and 2007. The firms in GCC have, therefore, been reducing the leverage since the 2008 financial crisis.

3.4 Results

In this section we present the results of the estimations for the models presented in the methodology section above. A Hausman test was conducted to decide whether to use fixed or random effects. The results showed that the test statistic was significant and therefore fixed effects estimation was preferred. The section below therefore presents the results of fixed effects estimations and Hausman test.

We are first looking at managerial ownership versus external ownership. Subsequently, we split managerial ownership to its components as CEO share and Chairman share versus external ownership. We also look at the interact CEO ownership and CEO family

as well as Chairman ownership and Chairman family to test whether CEO and Chairman from family makes a difference. Second we turn our attention to external ownership. We separate external ownership to two components as institutional

Table 3.4 Mean values of the variables by year

This table reports descriptive per year mean values of the variable used in the study. For ownership variables we do not report the values if shares owned is less than 5 per cent. All the variables are measured at the end of each year. Sources: Thomson one.com, Datastream and annual reports of the companies. Definitions for all the variables are provided in Table 3.1.

Variable	2006	2007	2008	2009	2010	2011
Performance measures						
Tobin's Q	2.42	2.40	1.77	1.60	1.62	1.58
Return on assets (ROA)	9.77	6.15	6.48	10.19	3.39	4.80
Board Characteristics						
CEOChair	0.50	0.51	0.50	0.50	0.50	0.50
Board size	7.13	7.14	7.16	7.19	7.19	7.19
Executive directors	0.79	0.77	0.77	0.77	0.75	0.74
Independent directors	5.46	5.48	5.50	5.53	5.45	5.42
Ownership Structure						
Managerial ownership	3.50	4.39	3.53	3.44	3.56	3.41
CEO ownership	0.00	0.40	0.32	0.44	0.58	0.55
CEO family	0.10	0.10	0.10	0.11	0.11	0.10
CEO family ownership	0.00	0.27	0.16	0.29	0.36	0.35
Chairman ownership	3.50	3.99	3.20	3.00	2.98	2.85
Chairman family	0.38	0.38	0.38	0.38	0.38	0.38
Chairman family ownership	3.50	3.63	2.99	2.35	2.29	2.16
Family ownership	32.50	6.91	6.06	5.45	5.48	5.43
Non-family ownership	12.12	5.71	6.32	7.05	7.05	7.23
External ownership	50.28	45.28	46.95	45.97	46.02	46.55
Institutional investor ownership	5.66	35.15	36.82	35.24	35.30	35.54
Domestic institutional ownership	0.00	1.58	1.68	1.44	1.46	1.51
Foreign institutional ownership	0.00	0.23	0.30	0.29	0.30	0.32
Non-governmental institutional ownership	5.66	29.60	30.46	28.85	29.09	29.51
Corporation ownership	5.66	22.26	23.75	21.68	22.18	22.88
Domestic corporation ownership	0.00	0.98	1.06	0.87	0.89	0.93
Foreign corporation ownership	0.00	0.02	0.04	0.03	0.04	0.05
Investment manager ownership	0.00	7.34	6.71	7.17	6.91	6.95
Domestic investment manager ownership	0.00	0.39	0.36	0.32	0.31	0.31
Foreign investment manager ownership	0.00	0.00	0.00	0.00	0.01	0.01
Individual investor ownership	44.62	12.49	12.31	12.46	12.49	12.66
Government ownership	0.00	5.55	6.36	6.39	6.54	6.35
Foreign ownership	0.50	0.13	0.23	0.35	0.37	0.38
Concentrated ownership	2209	1297	1194	1229	1192	1225
Financial and economic characteristics						
Leverage	0.21	0.21	0.24	0.23	0.22	0.23
Firm size	4.98	5.23	5.39	5.43	5.49	5.53
GDP growth	5.84	5.14	7.35	-0.76	4.73	7.72

ownership and individual ownership. Subsequently, we examine whether there is a difference between types of institutional investors and distinguish between institutional investors as corporate, investment management and government. Third, we look at family ownership versus non-family ownership, government ownership versus institutional ownership, foreign ownership versus institutional ownership and finally we look to concentrated ownership versus dispersed ownership.

3.4.1 Insider Ownership versus External Ownership

We start by running a baseline regression with aggregate ownership variables as managerial and external. Results are presented in Table 3.5 Model 1. We find that managerial ownership has a positive and statistically significant impact on Tobin's Q. This evidence is consistent with both theoretical and empirical arguments. Jensen and Meckling (1976) for example argue that insider ownership has a positive impact on firm performance. Consistent with Jensen and Meckling (1976) the positive impact of insider ownership on the Tobin's Q can be attributed to the fact that managerial ownership enables the interests of managers to be more aligned with those of shareholders, which in turn reduces agency problems and thus improves firm performance in the GCC countries[7].

The study is consistent with Han (2006) who investigate the impact of insider ownership on real estate investment trusts (REITs). The evidence is also consistent with Chen et al. (2005) who observe a positive and significant impact of insider ownership on firm performance in Japan as well as Drobetz et al. (2005) who show that insider ownership has a significant positive effect on firm performance in Switzerland. Furthermore, Gugler et al. (2008) employ an average Tobin's Q and a marginal Tobin's Q to show that insider ownership has a positive impact on firm performance in the US. These findings are consistent with the theoretical argument that insider ownership helps in aligning the interests of managers with those of shareholders (Jensen and Meckling, 1976). Our findings, however, contrast with Davies et al. (2005); Fernandez and Gomez

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[7] However, it is important to highlight that the analysis does not distinguish between the effectiveness of roles and the division of responsibilities between the CEO and the Chairman, who collectively lead and manage the strategic and operational policies and decisions of the companies.

Table 3.5 Managerial ownership and firm performance

This table presents coefficient estimates for fixed effects regressions estimating the relationship between corporate governance variables and performance using Tobin's Q as the dependent variable. Year dummy variables control for the macroeconomic conditions. Robust standard errors are reported in parenthesis. ***, ** and * represents significance levels at 1%, 5% and 10%, respectively. Definitions for all the variables are provided in Table 3.1.

	Model 1	Model 2	Model 3	Model 4	Model 5
Board Characteristics					
Board size	0.05	0.04	0.04	0.04	0.04
	(0.07)	(0.07)	(0.07)	(0.07)	(0.07)
Executive directors	-0.01	0.01	0.02	0.01	0.01
	(0.12)	(0.12)	(0.12)	(0.12)	(0.12)
Independent directors	-0.01	-0.01	-0.01	-0.01	-0.01
	(0.04)	(0.04)	(0.04)	(0.04)	(0.04)
Ownership Structure					
Managerial ownership	0.05**				
	0.02				
External ownership	0.00	0.00	0.00	0.00	0.00
	(0.00)	(0.00)	(0.00)	(0.00)	(0.00)
CEO ownership		0.08	0.15	0.08	0.15
		(0.05)	(0.65)	(0.05)	(0.65)
Chairman ownership		0.05**	0.05**	0.06	0.06
		(0.03)	(0.03)	(0.05)	(0.05)
CEO family ownership			-0.42		-0.42
			(0.69)		(0.69)
CEO family			6.41		6.41
			(4.17)		(4.18)
Chairman family ownership				-0.01	-0.01
				(0.06)	(0.06)
Chairman family				-0.02	-0.02
				(0.49)	(0.49)
Family ownership	-0.07***	-0.07***	-0.07***	-0.07***	-0.07***
	(0.02)	(0.02)	(0.02)	(0.02)	(0.02)
Firm Characteristics					
Firm size	-0.29*	-0.3**	-0.3**	-0.3**	-0.3**
	(0.14)	(0.14)	(0.14)	(0.14)	(0.14)
Leverage	-1.59***	-1.59***	-1.61***	-1.59***	-1.61***
	(0.36)	(0.36)	(0.36)	(0.36)	(0.36)
GDP growth	-0.02*	-0.02*	-0.02*	-0.02*	-0.02*
	(0.01)	(0.01)	(0.01)	(0.01)	(0.01)
Year dummy variables	Yes	Yes	Yes	Yes	Yes
Number of observations	1074	1074	1074	1074	1074
Number of groups	302	302	302	302	302
Hausman Test (P-value)	0.00	0.00	0.00	0.00	0.00

(2002); Firth et al. (2002); and Agrawal and Knoeber (1996) who fail to find a significant impact of managerial ownership on firm performance.

On the other hand, we do not find any significant relationship between external ownership, at an aggregate level and firm performance. Unlike insider ownership, external ownership does not play a significant role in monitoring the behaviour of managers. This explains why external ownership does not significantly influence the performance of firms in GCC countries. Later we will look at different external owners, such as institutional or governmental, but first we scrutinise the managerial ownership more. Establishing that managerial ownership has an impact on firm performance, we subsequently distinguish between CEO and Chairman ownership. Results are presented in Model 2 of Table 3.5. We find that Chairman ownership has a positive and significant impact on performance while the coefficient of CEO ownership is not statistically significant. The results can be attributed to the fact that the ownership of shares by the CEO or chairman improves the corporate governance structure of the firm. A CEO who owns shares will be interested in making decisions that will maximise the value of the firm. The CEO will try to ensure that the firm invests only in projects with positive net present value. Similar explanations can be given for the case of the chairman. A chairman who owns shares will also ensure that the strategic decisions taken by the firm are in line with shareholder value maximisation. In the context of GCC countries, the Chairman and CEO roles are often played by the same person. This means that the monitoring role of the Chairman and CEO are higher than for other countries such as the UK where the CEO and chairman roles are played by different people (FRC, 2012).

In the context of GCC countries, this result could be attributed to the corporate governance practices. In the GCC countries, the Chairman probably has a significant effect to play in monitoring the performance of firms. The ownership of shares by the Chairman increases the motivation of the Chairman to implement strategies that are in line with creating value for shareholders. Using an interaction variable, we also tested whether CEO and Chairman from the family has an impact on firm performance. This is important because a CEO or chairman from the family will have a different level of motivation. Such a CEO or chairman will see themselves as an owner rather than as an employee. There will thus be a greater alignment of the CEO or Chairman's interests with those of shareholders. Consequently, one should expect performance to be positive if the

chairman or CEO is a family member. This relationship is tested in Models 4 and 5 in Table 3.5. As can be observed, the performance is not affected by the fact that the CEO or chairman is a family member. The empirical evidence however does not support this finding. For example, Villalonga and Amit (2006) argue that firms in which the founder is active as CEO or chairman should perform well while those with descendants should perform worse. Furthermore, Pérez-González (2006) observes that inherited control has a negative effect on firm performance since in most cases the heir does is not aware of the challenges that the founder has encountered in the process of building the business.

We then turn our attention to external ownership. Firstly, we separate external ownership to two components as institutional ownership and individual ownership. Results are presented in Table 3.6 Model 6 and we find that institutional investor ownership has a positive and statistically significant impact on performance. This is consistent with the theoretical arguments that institutional investors are better placed to monitor the behaviour of investors and that they have access to better information. Institutional owners are more sophisticated, more professional and better informed (McConnell and Servaes, 1990; Han and Suk, 1998; Tsai and Gu, 2007). This may explain why their impact on firm performance in GCC countries is positive[8]. Subsequently, we examine whether there is a difference between types of institutional ownership and distinguish between institutional ownership as corporate, investment management and government. Results are presented in Model 7 of Table 3.6 and we find that only corporation ownership has a positive and significant impact on performance of GCC companies. Corporate owners have enough resources to monitor the behaviour of managers. By doing so, the interests of managers in firms with high corporation ownership are more aligned with those of shareholders. Consequently, firms with a high percentage of corporate owners will tend to perform better than those with a lower percentage of corporate owners (Han and Suk, 1998; Tsai and Gu, 2007). It is noteworthy that we do not find any significant relationship for governmental ownership. Government

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[8] These arguments are further strengthened by Hartzell and Starks (2003), who observe a negative relationship between managerial compensation and institutional ownership. This highlights the monitoring role played by institutional owners who ensure that managers are not compensated for work that has not been done.

Table 3.6 External ownership and firm performance

This table presents coefficient estimates for fixed effects regressions estimating the relationship between corporate governance variables and performance using Tobin's Q as the dependent variable. Year dummy variables control for the macroeconomic conditions. Robust standard errors are reported in parenthesis. ***, ** and * represents significance levels at 1%, 5% and 10%, respectively. See Table 3.1 for exact definitions of variables.

	Model 6	Model 7	Model 8	Model 9	Model 10
Board Characteristics					
Board size	0.05	0.06	0.06	0.07	0.06
	(0.07)	(0.07)	(0.07)	(0.07)	(0.07)
Executive directors	-0.01	-0.02	-0.01	-0.02	-0.02
	(0.12)	(0.12)	(0.12)	(0.12)	(0.12)
Independent directors	-0.01	-0.01	0.00	-0.01	-0.01
	(0.04)	(0.04)	(0.04)	(0.04)	(0.04)
Ownership Structure					
Institutional investor ownership	0.01**		0.00		
	(0.00)		(0.00)		
Individual investor ownership	0.01	0.01	0.01	0.01	0.01
	(0.01)	(0.01)	(0.01)	(0.01)	(0.01)
Corporation ownership		0.02***		0.01	0.02***
		(0.01)		(0.01)	(0.01)
Investment manager ownership		-0.01		-0.01	-0.01
		(0.01)		(0.01)	(0.01)
Government ownership		0.01		0.01	0.01
		(0.01)		(0.01)	(0.01)
Domestic institutional ownership			0.24**		
			(0.10)		
Foreign institutional ownership			0.08		
			(0.21)		
Domestic corporation ownership				0.24*	
				(0.13)	
Foreign corporation ownership				0.06	
				(0.44)	
Domestic investment manager ownership					-0.05
					(0.26)
Foreign investment manager ownership					0.17
					(0.84)
Managerial ownership	0.06**	0.06**	0.05**	0.05**	0.06**
	(0.02)	(0.02)	(0.02)	(0.02)	(0.02)
Family ownership	-0.08***	-0.08***	-0.08***	-0.08***	-0.08***
	(0.02)	(0.02)	(0.02)	(0.02)	(0.02)
Firm Characteristics					
Firm size	-0.29**	-0.29**	-0.3**	-0.29**	-0.29**
	(0.14)	(0.14)	(0.14)	(0.14)	(0.14)
Leverage	-1.6***	-1.61***	-1.62***	-1.61***	-1.61***
	(0.36)	(0.36)	(0.36)	(0.36)	(0.36)
GDP growth	-0.02	-0.02	-0.02*	-0.02	-0.02
	(0.01)	(0.01)	(0.01)	(0.01)	(0.01)
Year dummy variables	Yes	Yes	Yes	Yes	Yes
Number of observations	1074	1074	1074	1074	1074
Number of groups	302	302	302	302	302
Hausman Test (P-value)	0.00	0.00	0.01	0.00	0.00

ownership should normally have a negative effect in performance because government ownership tends to promote inefficiencies. For example, Huang and Xia (2012) observe that government ownership negatively affects firm performance in transition economies. Furthermore, La Porta et al. (2002) observes that government ownership hurts the performance of banks across 92 countries. Likewise, Dinc (2005); and Brown and Dinc (2005) observe a negative impact of government ownership on bank performance in the US. Governments in transition countries such as those in the GCC region tend to be characterised by high levels of corruption (Nowak, 2001). This means that the government will not play an effective role in monitoring the behaviour of corporate executives. The absence of a significant impact of government ownership on firm performance in the Gulf region can be explained by the fact that there is a threshold level at which government ownership influences performance. Government ownership does not influence performance below or above this threshold level (Tian and Estrin, 2005).

We also examine whether foreign institutional ownership in comparison to domestic makes a difference in performance in the GCC countries. We look at the number foreign and domestic institutional investors for each group. Results are presented in Models 8 to 10 in Table 3.6. We find that domestic institutional ownership has a positive and statistically significant impact on performance. This is also valid for domestic corporation ownership. This finding is consistent with the empirical evidence on institutional ownership and firm performance (e.g., McConnell and Servaes, 1990; Han and Suk, 1998; Tsai and Gu, 2007). From a theoretical perspective, institutional owners play an active role in monitoring the behaviour of managers (Hand, 1990). This is because institutional owners are more sophisticated, more professional, and have access to more information than individual shareholders. Institutional owners in GCC countries are probably playing an active role in monitoring the behaviour of the managers of firms in which they have vested their interests. Consistent with Hartzell and Starks (2003), domestic institutional owners in GCC countries have probably replaced incentive schemes aimed at aligning managerial interests with those of shareholders with between monitoring thus eliminating agency problems and improving the performance of firms in the GCC region. Also, this finding is supported by the findings of Al-Saidi and Al-Shammari (2013) in the GCC banking sector. Therefore, performance of GCC companies is affected by domestic institutional ownership.

Table 3.7 Family, government, foreign and concentrated ownership and firm performance

This table presents coefficient estimates for fixed effects regressions estimating the relationship between corporate governance variables and performance using Tobin's Q as the dependent variable. Year dummy variables control for the macroeconomic conditions. Robust standard errors are reported in parenthesis. ***, ** and * represents significance levels at 1%, 5% and 10%, respectively. Definitions for all the variables are provided in Table 3.1.

	Model 11	Model 12	Model 13	Model 14
Board Characteristics				
Board size	0.05	0.05	0.05	0.05
	(0.07)	(0.07)	(0.07)	(0.07)
Executive directors	-0.01	-0.01	-0.01	-0.01
	(0.12)	(0.12)	(0.12)	(0.12)
Independent directors	-0.01	0.00	-0.01	-0.01
	(0.04)	(0.04)	(0.04)	(0.04)
Ownership Structure				
Family ownership	-0.07***	-0.07***	-0.07***	-0.08***
	(0.02)	(0.02)	(0.02)	(0.02)
Non-family ownership	0.01			
	(0.01)			
Government ownership		0.01		
		(0.01)		
Non-governmental institutional ownership		0.01**		
		(0.00)		
Foreign ownership			0.18	
			(0.21)	
Institutional investor ownership	0.01**		0.01**	0.01**
	(0.00)		(0.00)	(0.00)
Concentrated ownership				0.00
				(0.00)
Individual investor ownership				0.01
				(0.01)
Managerial ownership	0.06**	0.06**	0.06**	0.06**
	(0.02)	(0.02)	(0.02)	(0.02)
Firm Characteristics				
Log firm size	-0.29**	-0.3**	-0.31**	-0.31**
	(0.14)	(0.14)	(0.14)	(0.14)
Leverage	-1.6***	-1.6***	-1.57***	-1.58***
	(0.36)	(0.36)	(0.36)	(0.36)
GDP growth	-0.02	-0.02	-0.02	-0.02*
	(0.01)	(0.01)	(0.01)	(0.01)
Year dummy variables	Yes	Yes	Yes	Yes
Number of observations	1074	1074	1074	1074
Number of groups	302	302	302	302
Hausman Test (P-value)	0.00	0.00	0.00	0.00

3.4.2 Family Ownership

In all models we control for family ownership as literature points out that this is an important characteristic of ownership in the GCC countries. We consistently find the coefficient of family ownership to be significant and has a negative impact on performance. This is contrary to Arosa et al. (2010) findings who argued that family ownership has a positive impact on firm performance. The finding also contrasts with earlier evidence by Anderson and Reeb (2003), Villalonga and Amit (2006), Maury (2006), Barontini and Caprio (2006), and Pindado et al. (2008). These studies support the theoretical argument that family owners tend to have greater incentives to monitor managers (agents) than other shareholders (Anderson and Reeb, 2003). This argument seems not to be supported from the perspective of the GCC region. The negative relationship could be as a result of the fact that family members in GCC countries are more interested in maximising their personal benefits rather than focusing on maximising shareholder wealth in general. Consequently decisions are made in such a way that favours family owners at the expense of a wider group of shareholders.

3.4.3 Government Ownership

Overall, in models where we employ government ownership we do not find a significant effect on performance. This evidence is inconsistent with most empirical and theoretical arguments. As mentioned earlier, Shleifer and Vishny (1997) argue that government ownership can have a negative effect on firm performance because government owned companies are often under excessive pressure to employ people even when resources are limited. Sun et al. (2002) supported the view that government ownership in developing countries puts positive effect on the firm performance. GCC countries can be regarded as emerging countries in which government has a positive role to play in the development of business. For example, Jefferson (1998); Stiglitz (1996) and Sun et al. (2002) argue that government ownership is important in emerging countries because it can facilitate the resolution of disputes relating to ambiguous property rights.

3.4.4 Foreign Ownership

Earlier we reported that foreign ownership does not have an impact on performance for separate institutional ownership categories. We also create an aggregate variable to test the impact of foreign ownership. Results are presented in Model 13 in Table 3.7 and we still find the coefficient of foreign ownership to be insignificant. The results are inconsistent with Arnold and Javorcik (2005), Petkova (2008); Girma (2005); Girma and Georg (2006); and Girma et al. (2007) who all observe that foreign ownership has a positive impact on firm performance. Furthermore, Arouri et al. (2014) find that foreign ownership maintains a significant positive association with the GCC banks performance.

Foreign ownership in GCC countries is limited. According to SMEInfo (2014) limitations to foreign ownership and punitive bankruptcy laws pose significant challenges to attracting foreign direct investment (FDI). In Oman for example, the Foreign Capital Investment Law of 1994 restricts foreign ownership to 49% (OECD, 2011). Given the restrictions on foreign ownership in the region, it is not surprising that foreign ownership has no significant effect on firm performance in the region.

3.4.5 Concentrated Ownership

We also examine how concentrated ownership may affect the performance in the GCC firms. Results, presented in Model 14 in Table 3.7, show that the coefficient of HI is not significant. This findings signals that performance of GCC companies is not affected by concentrated ownership. This is contrary to the findings of Almudehki and Zaitun (2012), who used Tobin's Q, ROE and ROA found that ownership concentration, has positive relation with firm performance. According to Zaitun, one can assess the level of ownership concentration by evaluating the investor protection and its impact on profit maximisation. The results are also inconsistent with the empirical evidence such as Grosfeld (2006); Holmstrom and Tirole (1993) who argue that concentrated ownership contributes to poor liquidity and as such negatively affects the performance of a firm. Furthermore, Demsetz and Lehn (1985) and Admati et al. (1994) argue that ownership concentration limits the ability of a firm to diversify. This means that foreign institutional

shareholders cannot buy large blocks of shares. This reduces the ownership concentration and thus limits the impact of concentrated ownership on firm performance in the region.

Table 3.8 Managerial ownership and firm profitability

This table presents coefficient estimates for fixed effects regressions estimating the relationship between corporate governance variables and performance using Return on Assets (ROA) as the dependent variable. Year dummy variables control for the macroeconomic conditions. Robust standard errors are reported in parenthesis. ***, ** and * represents significance levels at 1%, 5% and 10%, respectively. Definitions for all the variables are provided in Table 3.1.

	Model 1	Model 2	Model 3	Model 4	Model 5
Board Characteristics					
Board size	-0.91	-1.25	-1.27	-1.27	-1.29
	(0.98)	(0.99)	(1.00)	(1.00)	(1.00)
Executive directors	-1.36	-0.71	-0.68	-0.61	-0.59
	(1.81)	(1.85)	(1.85)	(1.86)	(1.86)
Independent directors	-0.12	-0.16	-0.16	-0.13	-0.13
	(0.57)	(0.57)	(0.57)	(0.57)	(0.57)
Ownership Structure					
Managerial ownership	-0.38				
	(0.30)				
External ownership	-0.05	-0.04	-0.04	-0.04	-0.04
	(0.04)	(0.04)	(0.04)	(0.04)	(0.04)
CEO ownership		0.78	2.05	0.83	2.03
		(0.73)	(9.30)	(0.73)	(9.31)
Chairman ownership		-0.49	-0.5*	-0.84	-0.84
		(0.30)	(0.31)	(0.68)	(0.69)
CEO family ownership			-4.45		-4.32
			(10.46)		(10.46)
CEO family			56.89		55.74
			(85.52)		(85.59)
Chairman family ownership				0.44	0.43
				(0.76)	(0.77)
Chairman family				6.33	6.31
				(7.15)	(7.15)
Family ownership	0.09	-0.01	0.00	-0.06	-0.04
	(0.30)	(0.30)	(0.30)	(0.31)	(0.31)
Firm Characteristics					
Firm size	-1.85	-1.94	-1.99	-1.86	-1.92
	(2.04)	(2.04)	(2.04)	(2.04)	(2.05)
Leverage	0.5	0.69	0.62	0.81	0.74
	(5.27)	(5.26)	(5.27)	(5.27)	(5.28)
GDP growth	0.17	0.14	0.14	0.14	0.14
	(0.2)	(0.2)	(0.2)	(0.2)	(0.2)
Year dummy variables	Yes	Yes	Yes	Yes	Yes
Number of observations	1035	1035	1035	1035	1035
Number of groups	305	305	305	305	305
Hausman Test (P-value)	0.80	0.69	0.81	0.75	0.85

3.4.6 Results with ROA as the performance measure

In this section we repeat the analysis above using the ROA as the performance measure. Results for the managerial ownership and external ownership are presented in Table 3.8. In Model 1 we observe that neither managerial ownership nor external ownership has significant coefficients. There have been arguments that managerial ownership gives managers control over the firm. This enables managers to gain performance incentives which should result in a positive effect of insider ownership on firm performance (Jensen and Meckling, 1976; Han, 2006). Our findings are similar to Himmelberg et al. (1999), who using Tobin's Q fail to find any significant impact of managerial ownership among U.S firms, and Davies et al. (2005), who fail to find any significant impact of managerial ownership on firm performance among UK firms. Davies et al. (2005) also used Tobin's Q to support their findings. McConnell and Servaes (1990) provide evidence of relationship between managerial ownership and firm performance. Similarly Davies et al. (2005) observe a relationship between managerial ownership and firm performance.

Subsequently, we employ CEO ownership and chairman ownership separately for managerial ownership in Model 2. We do not report any significant relationship for these variables. We then interact CEO ownership and chairman ownership with family CEO and chairmen. Again, here the relationships are not statistically significant.

We then turn our attention to institutional ownership and the results are presented in Table 3.9. In Model 6, we do not find a significant coefficient for institutional ownership. Looking at different institution owners in Model 7, we report that only government ownership is significant and negatively related to the ROA. This evidence is consistent with previous evidence on ownership structure which argues that government ownership is likely to have a negative impact because government ownership leads to an increase in inefficiencies in a firm. This finding contrasts with the finding obtained using the Tobin's Q. The evidence here suggests that there could be a contradiction in the manner in which Tobin's Q and ROA capture performance. As noted earlier, the ROA is a more accurate measure of performance because it forces managers to use the assets under their control to create wealth for shareholders. The Tobin's Q on the contrary makes managers to become myopic. The idea that

Table 3.9 External ownership and profitability

This table presents coefficient estimates for fixed effects regressions estimating the relationship between corporate governance variables and performance using Return on Assets (ROA) as the dependent variable. Year dummy variables control for the macroeconomic conditions. Robust standard errors are reported in parenthesis. ***, ** and * represents significance levels at 1%, 5% and 10%, respectively. See Table 3.1 for exact definitions of variables.

	Model 6	Model 7	Model 8	Model 9	Model 10
Board Characteristics					
Board size	-0.92	-0.84	-0.88	-0.79	-0.87
	(0.98)	(0.98)	(0.98)	(0.98)	(0.98)
Executive directors	-1.33	-1.33	-1.63	-1.39	-1.37
	(1.81)	(1.81)	(1.81)	(1.81)	(1.81)
Independent directors	-0.13	-0.20	-0.14	-0.22	-0.17
	(0.57)	(0.57)	(0.57)	(0.57)	(0.58)
Ownership Structure					
Institutional investor ownership	-0.07		-0.08		
	(0.06)		(0.06)		
Individual investor ownership	-0.06	-0.07	-0.06	-0.07	-0.07
	(0.12)	(0.12)	(0.12)	(0.12)	(0.12)
Corporation ownership		-0.08		-0.16*	-0.08
		(0.08)		(0.09)	(0.08)
Investment manager ownership		0.14		0.14	0.16
		(0.11)		(0.11)	(0.12)
Government ownership		-0.37**		-0.37	-0.37**
		(0.17)		(0.17)	(0.17)
Domestic institutional ownership			1.29		
			(1.57)		
Foreign institutional ownership			-5.76*		
			(3.20)		
Domestic corporation ownership				3.10	
				(2.00)	
Foreign corporation ownership				0.18	
				(6.35)	
Domestic investment manager ownership					-1.91
					(3.78)
Foreign investment manager ownership					-4.46
					(12.18)
Managerial ownership	-0.38	-0.36	-0.38	-0.38	-0.35
	(0.30)	(0.30)	(0.30)	(0.30)	(0.30)
Family ownership	0.10	0.09	0.11	0.1	0.08
	(0.31)	(0.31)	(0.31)	(0.31)	(0.31)
Firm Characteristics					
Firm size	-1.72	-1.44	-1.50	-1.45	-1.41
	(2.04)	(2.05)	(2.05)	(2.05)	(2.05)
Leverage	0.41	0.10	0.30	0.19	0.12
	(5.27)	(5.26)	(5.27)	(5.26)	(5.27)
GDP growth	0.16	0.15	0.15	0.13	0.16
	(0.20)	(0.20)	(0.20)	(0.20)	(0.20)
Year dummy variables	Yes	Yes	Yes	Yes	Yes
Number of observations	1035	1035	1035	1035	1035
Number of groups	305	305	305	305	305
Hausman Test (P-value)	0.83	0.58	0.76	0.54	0.62

government ownership results in inefficiencies can also be supported by theoretical and empirical evidence. For example, Sun and Tong (2003) provide evidence that government ownership negatively affects firm performance. Similarly Huang and Xiao (2012); La Porta et al. (2002); Dinc and Brown (2005), and Dinc (2005), observe that government ownership negatively affects firm performance. These studies provided evidence to their findings based on Tobin's Q. This evidence can be attributed to the fact that government owned firms often face political pressure for excessive employment (Shleifer and Vishny, 1997). The evidence is particularly consistent with Shleifer and Vishny (1997) who argue that government ownership can contribute to poor performance because state-owned enterprises are often under political pressure to employ more people. Consistent with this theory, one can attribute the negative impact of government ownership on firm performance to the state-owned firms in GCC countries, which have more employees than resources can permit witnessed in their labour sheet. The government companies, in order to fulfil their obligations to provide local citizens as prescribed by their respective governments, tend to employ more people. This is reflected by a negative relationship between government ownership and firm performance in GCC countries. The evidence, however, contrasts with theoretical arguments that government ownership can improve firm performance in emerging and less developed economies (e.g., Jefferson, 1998; Stiglitz, 1996; Sun et al., 2002).

The main support behind this argument is that government ownership can help in the resolution of issues regarding ambiguous property rights (Jefferson, 1998; Stiglitz, 1996; Sun et al., 2002). While government ownership is likely to improve performance in this area, the overall impact on performance in GCC countries is negative. The evidence is also consistent with some of the empirical findings on the relationship between state ownership and firm performance. For example, Xu and Wang (1999) observe a negative relationship between government ownership and firm performance in China. The evidence is also consistent with Sun and Tong (2003) who observe that government ownership negatively affects firm performance in China as well as Delios and Wu (2005); Huang and Xiao (2012); La Porta et al. (2002); Dinc (2005) and Brown and Dinc (2005). However, Sun et al. (2002) provide contrary results to those observed in this study based on data over the period 1994 to 1997.

In Model 9 we find that corporation ownership has a negative and statistically significant impact on ROA. These findings are not in line with the theoretical arguments that institutional investors are better placed to monitor the behaviour of investors and that they have access to better information (e.g., McConnell and Servaes, 1990; Han and Suk, 1998; Tsai and Gu, 2007). We also find, in Model 8 in Table 3.9, foreign institutional ownership has a negative and significant impact on ROA. These findings contradict with the outcomes of Arouri et al. (2014). Arouri et al. (2014) carried out an empirical analysis of ownership structure and firm performance in the GCC banking sector. Their findings reveal that institutional ownership has a positive impact on bank performance. The evidence is however, consistent with Hartzell and Starks (2003) who observe a negative link between managerial ownership and firm performance. Similarly, Pound (1988) and Hand (1990) provide evidence that managerial ownership negatively affects performance. The negative link between managerial ownership and firm performance in GCC countries can be attributed to the ability of the institutional investors to replace incentive schemes aimed at aligning the interest of managers with those of shareholders with better monitoring (Almudehki & Zeitun 2012). By eliminating managerial incentives, managers may not be motivated to implement strategies that will maximize shareholder wealth. In addition, it has been argued that institutional owners favour the achievement of short-term objectives. This means that institutional owners can force managers to focus on achieving short-term performance targets instead of focusing on achieving the long-term strategic goals of the firm (Porter, 1992; Coffee, 1991; Badrinath et al., 1989).

Looking at the family ownership in Model 11 in Table 3.10, we do not find any significant relationship between ownership structure and ROA. In models 13 and 14 in Table 3.10, the findings show that the relationship between the Return on Assets and foreign ownership is not significant. Likewise, no significant relationship exists between ownership concentration and ROA. This indicates that concentrated ownership and foreign ownership do not significantly influence the ROA of firms in GCC countries. In the context of the GCC region, foreign ownership is unlikely to influence performance because of the restrictions on foreign ownership (OECD, 2011; SMEInfo, 2014). Furthermore, the lack of a relationship between ROA and concentrated ownership is in contrast to the empirical evidence. For example, Grossfeld (2006) and Kapopoulos and

Table 3.10 Family, government, foreign and concentrated ownership and profitability

This table presents coefficient estimates for fixed effects regressions estimating the relationship between corporate governance variables and performance using Return on Assets (ROA) as the dependent variable. Year dummy variables control for the macroeconomic conditions. Robust standard errors are reported in parenthesis. ***, ** and * represents significance levels at 1%, 5% and 10%, respectively. Definitions for all the variables are provided in Table 3.1.

	Model 11	Model 12	Model 13	Model 14
Board Characteristics				
Board size	-0.92	-0.78	-0.90	-0.92
	(0.98)	(0.98)	(0.98)	(0.98)
Executive directors	-1.33	-1.39	-1.4	-1.32
	(1.81)	(1.81)	(1.82)	(1.82)
Independent directors	-0.13	-0.22	-0.14	-0.13
	(0.57)	(0.57)	(0.57)	(0.57)
Ownership Structure				
Family ownership	0.04	0.03	0.05	0.08
	(0.29)	(0.29)	(0.29)	(0.31)
Non-family ownership	-0.06			
	(0.12)			
Government ownership		-0.35**		
		(0.17)		
Non-governmental institutional ownership		-0.03		
		(0.06)		
Foreign ownership			-2.43	
			(3.07)	
Institutional investor ownership	-0.07		-0.07	-0.06
	(0.06)		(0.06)	(0.06)
Concentrated ownership				0.00
				(0.00)
Individual investor ownership				-0.04
				(0.13)
Managerial ownership	-0.38	-0.39	-0.41	-0.38
	(0.30)	(0.30)	(0.30)	(0.30)
Firm Characteristics				
Log firm size	-1.72	-1.58	-1.56	-1.78
	(2.04)	(2.04)	(2.04)	(2.05)
Leverage	0.41	0.15	0.11	0.52
	(5.27)	(5.26)	(5.27)	(5.28)
GDP growth	0.16	0.15	0.13	0.15
	(0.20)	(0.20)	(0.20)	(0.20)
Year dummy variables	Yes	Yes	Yes	Yes
Number of observations	1035	1035	1035	1035
Number of groups	305	305	305	305
Hausman Test (P-value)	0.83	0.64	0.79	0.81

Lazaretou (2006) observe a positive impact of concentrated ownership on firm performance.

3.4.7 Robustness Check:

3.4.7.1 Lagged variables:

To check the robustness of our results, we repeat our results of the estimations for the fixed effects regressions models with lagged values for independent firm characteristics variables. First, in Table 3.12 (Appendix A), we re-estimate the fixed effects regressions models with lagged values for firm characteristics variables for checking the robustness of findings in respect managerial ownership and firm performance. We find that the results of the robustness checks strongly support the findings from the original fixed effects regression. The coefficients from the robustness check in respect of all firm characteristic variables have shown the same trend. For example, the coefficients for board size in the robustness check have not deviated much from those of the original regression. However, in the case of the variable of leverage with one year lag value, the robustness check indicates more significant negative correlation with the dependent variable of firm performance where a significant deviation from the original finding is observed.

Second, we re-estimate the fixed effects regressions models with lagged values for firm characteristics variables for checking the robustness of findings in respect external ownership and firm performance. The results of the robustness check are presented in Table 3.13 (Appendix A). The findings show a slight variation in the correlation between domestic and foreign investment manager ownership and firm performance. The negativity in relationship was found more in the case of domestic investment manager ownership and the positivity in the case of foreign manager ownership has come down in the robustness check. In the case of firm size and leverage using one year lag values the findings show significant variations with the negativity in both the variables. These two variables show significantly lesser negative relationship with firm performance when tested for the robustness using lagged values.

Finally, we re-estimate the fixed effects regressions models with lagged values for firm characteristics variables for checking the robustness of findings in respect family, government, foreign and concentrated ownership and firm performance. Findings of the robustness check using lagged values are shown in Table 3.14 (Appendix A). We find that the findings of robustness check strongly support the findings from the original empirical tests except in the case of foreign ownership where a slight variation from the original finding is noticed. Further, in the case of the variables firm size and leverage where one year lag values are used, significantly lesser negative relationship with firm performance is reported in the robustness check.

3.5 Conclusion

This paper looks at whether ownership structure has an impact on firm performance in GCC countries. This region has witnessed significant economic growth over the last few decades. The region is also facing turbulent times with respect to corporate governance practices, resulting in poor firm performance. Corporate governance issues are not limited to the Gulf region. From a global point of view, corporate governance has witnessed significant transformations over the last decade (Gomez and Korine, 2005). The data used in this study includes 305 non-financial listed firms from five GCC countries during the period of 2006-2011. We use Tobin's Q and ROA as measures of firm performance. Controlling for board structure, firm characteristics and some macroeconomic variables, we examine the relationship between ownership and performance. The types of ownership structure that are include managerial ownership, family ownership, government ownership, institution ownership, foreign ownership and concentrated ownership.

The findings based on Tobin's Q provide evidence to prove a positive association between the shareholding patterns and financial performance of the companies selected for the study. For example, the study finds a significant positive association between insider ownership (managerial ownership) and performance of companies operating in the GCC region. The findings of this study are comparable with many other previous empirical studies that have used Tobin's Q as a measure of performance. From the findings it is

observed that the impact of managerial ownership is significant at 5% level, whereas the external ownership does not seem to have any influence on the firm performance.

The scope of the study covered the impact of different complements of managerial ownership like Chairman own share and a comparison of such impact as against external ownership. The findings provide evidence to prove the positive impact of Chairman own shares on firm performance in the context of GCC companies. On the other hand, the results show a negative association between CEO family and chairman family share ownership and firm performance in respect of the sample firms. The negativity of this relationship is found to be statistically insignificant implying negligible contribution of this component of ownership to firm performance levels.

Study of the impact of external ownership on firm performance with its components of institutional and individual ownership in GCC companies was also covered by this research. According to the empirical findings of this study the institutional investors and corporation ownership are found to influence the sample firms' performance to a large extent. The study has recorded statistically significant findings in this respect. According to the findings of the study, there is an enhanced level of performance by the GCC firms with institutional ownership (domestic and corporate domestic). This finding is consistent with the findings of some of the previous studies. The study has not observed any positive association between government ownership and the performance of GCC companies.

The study has observed a negative association between family ownership and the performance of sample firms selected for the study. This finding appears to be contradicting the findings in this respect by the earlier studies. From a theoretical perspective, family ownership is expected to contribute to better performance of firms because of their expertise. However, the findings of this study do not appear to support this proposition as no positive impact between the variables has been observed by the study. Contrary to the findings of earlier studies any association between government ownership and enhanced firm performance by the GCC companies has not been observed by the study. According to the empirical findings of this study, foreign ownership and concentrated ownership has no impact on firm performance in GCC firms.

The study also used ROA as a measure to assess the impact of ownership structure on firm performance. When the variable of ROA is used, the study was unable to provide any evidence to prove a significant and positive impact of ownership structure on the performance of sample GCC firms. Different components of ownership like chairman own share, corporate own, institutional owner foreign and government ownership all have negative effects on ROA in GCC countries.

In order to check the robustness of the findings from the fixed effects regression models undertaken as a part of this empirical research, this study carried out a robustness check using lagged values for independent firm characteristic variables. While the robustness check results indicated more significant negative correlation in the case of leverage, not much variation has been observed in the variable board size while checking for managerial ownership and firm performance. Similarly, while the negativity in the relationship between domestic investment manager owners increased positivity in the case of foreign manager was observed while checking for the impact of external ownership on firm performance. The findings of robustness check also showed a strong support to the findings from the original empirical tests in the case of foreign ownership.

This study has certain limitations that would render the findings to apply subject to the consideration of such limitations. From the published accounts of the sample firms, it was possible to gather information only on the number of foreign shareholders. The information does not reveal the percentage of foreign shareholdings as it is not mandatory to provide this information in the published accounts. The data contained ownership details in respect of shareholdings in excess of 5% of the total shareholdings of any firm under study as the firms in GCC countries report on the shareholdings that are either greater than or equal to 5%. Lack of details about smaller shareholdings might vitiate the findings to some extent. In addition, some of the firms in GCC countries do not have the practice of reporting all information relating to their shareholding patterns. Therefore, the fact that some of the ownership details with respect to certain firms in some years might be missing is to be recognised. The study is limited only to GCC countries. This means that the results cannot be generalised to other countries taking into account structural differences in the economies of other countries from those of GCC countries.

Further research can be conducted to examine the changes in the ownership structures because of changes in the market conditions and changes in government policies and consequent impact on the performance of companies. A comparative study of the impact of ownership structure on firm performance in one of the GCC countries with that of another developing country will prove to be beneficial from the extension of knowledge point of view.

Appendix A

Table 3.11 Correlation matrix

This table reports the correlation matrix for the variables that are used in the study. For ownership variables we do not report the values if shares owned is less than 5 per cent. All the variables are measured at the end of each year. Sources: Thomson one.com, Datastream and annual reports of the companies. Definitions for all the variables are provided in Table 3.1.

Columns are numbered (1)–(33) corresponding to the row variables in the same order.

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)	(14)	(15)	(16)	(17)	(18)	(19)	(20)	(21)	(22)	(23)	(24)	(25)	(26)	(27)	(28)	(29)	(30)	(31)	(32)	(33)
(1) CEOChair	1.00																																
(2) Board size	0.18	1.00																															
(3) Executive directors	0.05	0.28	1.00																														
(4) Independent directors	0.07	0.50	-0.27	1.00																													
(5) Leverage	0.06	-0.01	-0.09	0.06	1.00																												
(6) Tobin's Q	-0.19	-0.34	-0.12	-0.01	-0.12	1.00																											
(7) ROA	0.00	-0.01	0.00	0.00	0.01	0.04	1.00																										
(8) GDP growth	0.03	0.18	0.06	0.22	0.02	-0.13	-0.04	1.00																									
(9) Firm size	0.17	0.32	0.21	0.05	0.16	-0.15	-0.06	0.02	1.00																								
(10) Managerial ownership	0.01	0.02	0.31	-0.21	0.00	-0.04	0.01	-0.02	0.08	1.00																							
(11) CEO ownership	0.03	0.06	0.20	-0.12	-0.05	0.00	0.04	0.00	-0.07	0.30	1.00																						
(12) CEO family	-0.06	-0.03	0.20	-0.13	0.01	0.05	0.01	-0.02	0.05	0.21	0.31	1.00																					
(13) CEO family ownership	0.01	0.03	0.19	-0.10	-0.07	0.03	0.05	-0.01	-0.03	0.26	0.80	0.42	1.00																				
(14) Chairman ownership	0.00	0.01	0.27	-0.19	0.01	-0.04	0.00	-0.02	0.10	0.97	0.04	0.14	0.06	1.00																			
(15) Chairman family	-0.07	-0.04	0.07	-0.01	0.03	0.06	0.01	0.05	-0.08	0.28	0.11	0.40	0.10	0.26	1.00																		
(16) Chairman family ownership	-0.01	-0.03	0.23	-0.17	0.03	0.00	-0.01	-0.02	0.10	0.89	0.04	0.17	0.07	0.92	0.33	1.00																	
(17) Family ownership	-0.03	-0.10	0.11	-0.17	-0.01	-0.01	0.00	-0.06	-0.12	0.31	0.15	0.29	0.21	0.29	0.28	0.31	1.00																
(18) Non-family ownership	0.02	0.12	0.15	-0.11	-0.01	-0.11	0.00	-0.03	0.01	0.48	0.12	-0.03	-0.01	0.47	0.08	0.39	-0.14	1.00															
(19) External ownership	-0.05	-0.14	-0.14	-0.05	0.04	0.14	-0.06	-0.01	-0.08	0.09	-0.04	0.00	-0.05	0.10	0.05	0.13	0.16	0.11	1.00														
(20) Institutional investor ownership	-0.05	-0.19	-0.27	0.09	0.01	0.24	-0.06	0.02	-0.05	-0.25	-0.08	-0.11	-0.03	-0.24	-0.09	-0.19	-0.21	-0.33	0.67	1.00													
(21) Non-governmental institutional ownership	-0.05	-0.24	-0.19	0.06	0.06	0.27	-0.02	0.04	-0.13	-0.18	-0.04	-0.09	0.00	-0.18	0.01	-0.13	-0.14	-0.30	0.56	0.84	1.00												
(22) Domestic institutional ownership	-0.13	-0.17	-0.08	0.04	-0.01	0.37	-0.02	-0.05	-0.07	-0.17	-0.02	-0.09	0.04	-0.17	-0.01	-0.12	-0.07	-0.21	0.28	0.49	0.50	1.00											
(23) Foreign institutional ownership	0.02	0.20	-0.08	0.11	0.02	-0.04	-0.05	-0.03	0.16	-0.18	-0.11	-0.11	-0.08	-0.16	-0.21	-0.15	-0.15	-0.03	0.05	0.18	-0.17	0.09	1.00										
(24) Corporation ownership	-0.11	-0.28	-0.21	0.01	0.03	0.28	-0.01	-0.06	-0.23	-0.18	-0.09	-0.11	-0.06	-0.17	-0.04	-0.13	-0.17	-0.26	0.48	0.69	0.82	0.39	-0.11	1.00									
(25) Domestic corporation ownership	-0.12	-0.23	-0.10	0.01	-0.04	0.35	-0.01	-0.08	-0.16	-0.15	-0.08	-0.08	-0.05	-0.13	-0.02	-0.10	-0.12	-0.19	0.23	0.37	0.49	0.77	-0.18	0.62	1.00								
(26) Foreign corporation ownership	0.04	0.05	-0.05	0.01	0.08	0.03	0.00	0.02	-0.02	-0.06	-0.04	-0.02	-0.03	-0.05	-0.02	-0.05	-0.01	-0.07	0.02	0.10	0.05	-0.03	0.49	0.10	-0.04	1.00							
(27) Investment manager ownership	0.10	0.04	0.02	0.08	0.06	0.01	-0.02	0.17	0.14	-0.01	0.08	0.03	0.11	-0.03	0.10	-0.01	0.04	-0.09	0.17	0.30	0.35	0.22	-0.10	-0.23	-0.17	-0.08	1.00						
(28) Domestic investment manager ownership	-0.04	-0.07	0.07	-0.01	0.04	0.15	0.03	0.05	0.00	0.04	0.15	0.05	0.20	0.00	0.15	0.03	0.17	-0.06	0.11	0.18	0.24	0.50	-0.14	-0.15	-0.05	-0.07	0.67	1.00					
(29) Foreign investment manager ownership	0.07	0.07	0.19	-0.02	0.03	-0.04	0.01	0.01	0.04	0.02	-0.01	0.11	-0.01	0.03	0.03	-0.02	0.04	0.01	-0.04	-0.07	-0.06	-0.07	0.15	-0.05	-0.06	0.06	-0.01	-0.03	1.00				
(30) Individual investor ownership	-0.01	0.01	0.20	-0.22	-0.01	-0.10	0.00	-0.07	-0.09	0.59	0.20	0.21	0.16	0.57	0.28	0.53	0.71	0.60	0.21	-0.41	-0.33	-0.20	-0.15	-0.33	-0.23	-0.04	-0.03	0.09	0.03	1.00			
(31) Government ownership	0.00	0.10	-0.16	0.06	-0.09	-0.05	-0.07	-0.03	0.14	-0.14	-0.08	-0.05	-0.06	-0.13	-0.17	-0.11	-0.13	-0.07	0.21	0.31	-0.23	0.00	0.61	-0.21	-0.19	0.08	-0.05	-0.11	-0.02	-0.16	1.00		
(32) Foreign ownership	0.04	0.00	-0.11	0.07	0.09	-0.14	-0.02	0.02	-0.24	-0.05	-0.06	-0.06	-0.07	-0.03	-0.04	-0.01	0.16	0.03	0.13	0.03	0.03	-0.15	0.13	0.07	-0.08	0.26	-0.06	-0.15	0.09	0.15	0.03	1.00	
(33) Concentrated ownership	0.02	-0.04	-0.08	0.00	0.03	-0.07	-0.07	0.08	0.11	0.10	-0.06	-0.02	-0.06	0.13	0.00	0.15	-0.10	0.08	0.56	0.54	0.36	-0.15	0.11	0.23	-0.21	-0.03	0.25	-0.04	-0.04	-0.03	0.37	-0.01	1.00

Table 3.12 Managerial ownership and firm performance-Lagged Firm Characteristics

This table presents coefficient estimates for fixed effects regressions estimating the relationship between corporate governance variables and performance using Tobin's Q as the dependent variable. Year dummy variables control for the macroeconomic conditions. Robust standard errors are reported in parenthesis. ***, ** and * represents significance levels at 1%, 5% and 10%, respectively. Definitions for all the variables are provided in Table 3.1.

	Model 1	Model 2	Model 3	Model 4	Model 5
Board Characteristics					
Board size	0.056	0.048	0.043	0.048	0.043
	(0.068)	(0.070)	(0.070)	(0.070)	(0.070)
Executive directors	-0.004	0.010	0.017	0.010	0.018
	(0.121)	(0.123)	(0.123)	(0.124)	(0.124)
Independent directors	-0.013	-0.015	-0.013	-0.014	-0.013
	(0.039)	(0.039)	(0.039)	(0.039)	(0.039)
Ownership Structure					
Managerial ownership	0.058*				
	(0.025)				
External ownership	0.004	0.004	0.004	0.004	0.005
	(0.003)	(0.003)	(0.003)	(0.003)	(0.003)
CEO ownership		0.083	0.357	0.084	0.356
		(0.051)	(0.701)	(0.051)	(0.702)
Chairman ownership		0.054*	0.053*	0.050	0.050
		(0.026)	(0.026)	(0.048)	(0.048)
CEO family ownership			-0.607		-0.606
			(0.739)		(0.740)
CEO family			6.102		6.105
			(4.237)		(4.243)
Chairman family ownership				0.005	0.005
				(0.057)	(0.057)
Chairman family				-0.038	-0.040
				(0.526)	(0.526)
Family ownership	-0.070**	-0.071***	-0.071**	-0.072**	-0.071**
	(0.021)	(0.021)	(0.021)	(0.023)	(0.023)
Firm Characteristics					
Firm size (1 year lag)	-0.079	-0.079	-0.086	-0.080	-0.086
	(0.099)	(0.099)	(0.099)	(0.099)	(0.099)
Leverage (1 year lag)	-0.821*	-0.819*	-0.839*	-0.818*	-0.838*
	(0.331)	(0.331)	(0.331)	(0.332)	(0.332)
GDP growth	-0.011	-0.012	-0.012	-0.012	-0.012
	(0.014)	(0.014)	(0.014)	(0.014)	(0.014)
Year dummy variables	Yes	Yes	Yes	Yes	Yes
Number of observations	1,055	1,055	1,055	1,055	1,055
Number of groups	301	301	301	301	301

Table 3.13 External ownership and firm performance-Lagged Firm Characteristics

This table presents coefficient estimates for fixed effects regressions estimating the relationship between corporate governance variables and performance using Tobin's Q as the dependent variable. Year dummy variables control for the macroeconomic conditions. Robust standard errors are reported in parenthesis. ***, ** and * represents significance levels at 1%, 5% and 10%, respectively. See Table 3.1 for exact definitions of variables.

	Model 6	Model 7	Model 8	Model 9	Model 10
Board Characteristics					
Board size	0.059	0.066	0.065	0.071	0.066
	(0.068)	(0.068)	(0.068)	(0.068)	(0.068)
Executive directors	-0.012	-0.018	-0.012	-0.023	-0.018
	(0.120)	(0.120)	(0.120)	(0.120)	(0.120)
Independent directors	-0.012	-0.015	-0.011	-0.016	-0.016
	(0.039)	(0.039)	(0.039)	(0.039)	(0.039)
Ownership Structure					
Institutional investor ownership	0.009*		0.004		
	(0.004)		(0.004)		
Individual investor ownership	0.015	0.016	0.015	0.016	0.016
	(0.010)	(0.010)	(0.010)	(0.010)	(0.010)
Corporation ownership		0.017**		0.010	0.017**
		(0.005)		(0.006)	(0.005)
Investment manager ownership		-0.006		-0.005	-0.005
		(0.008)		(0.008)	(0.008)
Government ownership		0.012		0.013	0.012
		(0.012)		(0.012)	(0.012)
Domestic institutional ownership			0.241*		
			(0.104)		
Foreign institutional ownership			0.046		
			(0.214)		
Domestic corporation ownership				0.252	
				(0.130)	
Foreign corporation ownership				0.007	
				(0.442)	
Domestic investment manager ownership					-0.122
					(0.264)
Foreign investment manager ownership					0.117
					(0.848)
Managerial ownership	0.059*	0.060*	0.055*	0.056*	0.061*
	(0.025)	(0.025)	(0.025)	(0.025)	(0.025)
Family ownership	-0.085***	-0.086***	-0.081***	-0.084***	-0.087***
	(0.024)	(0.024)	(0.024)	(0.024)	(0.024)
Firm Characteristics					
Firm size (1 year lag)	-0.074	-0.058	-0.074	-0.064	-0.059
	(0.099)	(0.099)	(0.099)	(0.099)	(0.099)
Leverage (1 year lag)	-0.765*	-0.776*	-0.806*	-0.791*	-0.773*
	(0.331)	(0.329)	(0.330)	(0.329)	(0.330)
GDP growth	-0.010	-0.009	-0.012	-0.011	-0.009
	(0.014)	(0.014)	(0.014)	(0.014)	(0.014)
Year dummy variables	Yes	Yes	Yes	Yes	Yes
Number of observations	1,055	1,055	1,055	1,055	1,055
Number of groups	301	301	301	301	301

Table 3.14 Family, government, foreign and concentrated ownership and firm performance-Lagged Firm Characteristics

This table presents coefficient estimates for fixed effects regressions estimating the relationship between corporate governance variables and performance using Tobin's Q as the dependent variable. Year dummy variables control for the macroeconomic conditions. Robust standard errors are reported in parenthesis. ***, ** and * represents significance levels at 1%, 5% and 10%, respectively. Definitions for all the variables are provided in Table 3.1.

	Model 11	Model 12	Model 13	Model 14
Board Characteristics				
Board size	0.059	0.055	0.055	0.059
	(0.068)	(0.068)	(0.068)	(0.068)
Executive directors	-0.012	-0.007	-0.001	-0.010
	(0.120)	(0.120)	(0.120)	(0.120)
Independent directors	-0.012	-0.012	-0.012	-0.012
	(0.039)	(0.039)	(0.039)	(0.039)
Ownership Structure				
Family ownership	-0.070***	-0.068**	-0.068**	-0.086***
	(0.021)	(0.021)	(0.021)	(0.024)
Non-family ownership	0.015			
	(0.010)			
Government ownership		0.011		
		(0.012)		
Non-governmental institutional ownership		0.010*		
		(0.004)		
Foreign ownership			0.225	
			(0.210)	
Institutional investor ownership	0.009*		0.009*	0.010*
	(0.004)		(0.004)	(0.005)
Concentrated ownership				-0.000
				(0.000)
Individual investor ownership				0.016
				(0.010)
Managerial ownership	0.059*	0.062*	0.061*	0.059*
	(0.025)	(0.025)	(0.025)	(0.025)
Firm Characteristics				
Firm size (1 year lag)	-0.074	-0.077	-0.084	-0.078
	(0.099)	(0.099)	(0.099)	(0.099)
Leverage (1 year lag)	-0.765*	-0.793*	-0.754*	-0.749*
	(0.331)	(0.330)	(0.332)	(0.333)
GDP growth	-0.010	-0.009	-0.007	-0.011
	(0.014)	(0.014)	(0.014)	(0.014)
Year dummy variables	Yes	Yes	Yes	Yes
Number of observations	1,055	1,055	1,055	1,055
Number of groups	301	301	301	301

Chapter 4. Determinants of Executive Compensation in the GCC Countries

Abstract

This study explores the key determinants of the executive compensation in the GCC countries analysing a sample of 349 companies across industries for the period between 2006 and 2011. The study distinguishes between bonus and salaries paid to top five executives and it also examines the choice of compensation methods by GCC firms. The research finds that in the GCC countries larger firms and firms with potential future growth pay higher total compensation to their executives. Concentrated ownership structure leads to lower compensation levels while firms with high family ownership tend to pay higher compensation. There is also evidence that external ownership leads to higher total compensation. In terms of behaviour-oriented compensation (i.e. salary), we find that larger firms and firms with higher leverage pay higher salaries to executives. Firms that have a chairman from the family and have higher presence of executive members in the board tend to pay lower salaries. It is also found that managerial as well as institutional ownership of companies tends to lead to higher salaries. In terms of outcome-oriented compensation (i.e. bonus) the research finds evidence that companies that has more growth potential pay higher bonuses. A family related chairman and higher number of executive members in the board is related positively to bonus payments. There is also evidence that ownership by managers and by family results in higher levels of outcome-oriented compensation. The findings also indicate that the choice between behaviour versus outcome oriented compensation is mainly influenced by firm size, the presence of executive members on the board and managerial ownership. Companies that have higher number of executives or owned by managers pay more compensation through bonuses.

4.1 Introduction

Executive compensation is defined as a combination of rewards offered and given to the top executives (Deb, 2009). The combination of rewards includes both financial and non-financial types that are provided for the short and long run. Among other things, the rewards include salary, annual bonus, and other benefits that are given to the executives (Towers, 2001). Within this context, the executive compensation is broadly classified into four aspects as terminal benefits, performance-related compensation, base compensation and perquisites (Deb, 2009). Each has its own sub-categories including their duration, conditions and subsequent effect on executive performance. For example, the top executives receive or entitled to receive a very considerable pay including bonuses, incentives, share options and perks.

Executive compensation has been one of the aspects of modern day businesses that is being studied and analysed extensively. There is an ongoing debate on the elements that determine the executive pay levels and structures. Many theories are used to explain the executive compensation policies of corporate entities. However, the contracting approach of agency theory as explained by Jensen and Meckling (1976) has been one of the predominant theoretical approaches that are used to explain the basis of executive compensation. Agency theory argues that shareholders' interests in the corporations can be protected by monitoring the behaviour of managers closely, and such monitoring can be achieved by separating the ownership and control. Agency problem affecting the interests of shareholders are likely to arise because of the opportunities and incentives available to the managers to act in their own interest (Jensen and Meckling, 1976). Monitoring of the actions of the top executives becomes strategic decisions pertaining to the internal and external investment opportunities and financing. The operations are mostly contemplated and taken by the senior management. It has been observed that the executive directors consider and pursue those investment opportunities which serve the personal interests of the executive directors rather than satisfying the prime organisational objectives (Zhang, 2012). This situation may give rise to agency problems in the management of companies.

Following the findings of Jensen and Meckling (1976) that agency problems can also arise because of corporate governance issues, a large body of literature have highlighted the relationship between corporate governance and fixation of executive compensation; however, these studies have revealed that higher levels of executive compensation may not necessarily contribute to reduced levels of agency problems. According to Core et al. (1999), firms having weak governance structures are most likely to have higher compensation levels. This is because of the self-serving nature of executives which would induce them to undertake activities that would enable them to increase their own resources. Kim and Nofsinger (2007) found the need to have adequate corporate governance mechanisms in addition to executive compensation incentives in order to solve agency problems. The question as to whether market-based corporate governance mechanisms on executive compensation that are successful in developed countries would be effective in emerging economies like GCC countries remains debatable, especially in the light of nascent nature of corporate governance mechanisms prevalent in GCC countries. This makes the subject matter of this study – being the study of the determinants of executive compensation in these countries – more interesting and appropriate.

Executive compensation in general is construed to be an instrument to alleviate agency problems and to align the interests between the shareholders and management (Bebchuk and Fried, 2004). The dominance of the application of agency theory with respect to executive compensation is also subjected to criticism on the basis that the incentives may often lead to other outcomes and the effectiveness of managerial incentives may also be influenced by factors that are not considered by the agency theory (Hodgson, 1988). Although agency theory presupposes an alignment between firm performance and executive compensation, the findings from the previous studies are mixed. For example, some studies have found weak relationships between executive compensation and firm performance (e.g. Barkema and Gomez-Mejia, 1998; Jensen and Murphy, 1990). Other studies have found a strong association between these two factors (Kaplan, 2008; Hall and Liebman, 1998). In the context of the GCC countries, where there exists a large number of family-run companies, the level and structure of executive compensation is likely to differ widely offering an interesting research opportunity to examine the determinants of executive compensation, which is the central focus of this study.

A considerable amount of research has been carried out in the United Kingdom and the United States on executive compensation. For example, in the United Kingdom, Department for Business Innovation and Skills (2011) has discussed and issued paper on executive remuneration and its constituent parts, aspects, implications for shareholders and stakeholders. World at Work (2009) has also issued paper on executive compensation case studies. Similarly, International Labour Organization (2013) has issued a paper detailing the macro and micro aspects and impacts of executive compensation on the poor and the rich classes around the world. Within this context, the Greenbury Report (1995) has recommended that the firms should replace executive share options with conditional executive share options including long term incentives. The ultimate objective of this change is to ensure that the corporate performance must exist to validate the true efforts made by all executives.

In the United States, the Sarbanes-Oxley Act in 2002 drafted and recommended that accounting practices and policies, pertaining to top executives, should be strongly regulated. Despite these recommendations, the corporate governance practices have not changed significantly, instead more sophisticated corporate manoeuvring in the shape of corporate scandals is designed and carried out in a way to show artificial adherence to the corporate governance framework for only serving the vested interests of the executive directors at the cost of practical corporate performance (Giroux, 2006). The bankruptcy of Lehman Brothers in 2008 has validated the actual type of corporate governance practices in the United States (Harress and Caulderwood, 2013). For example, Porac et al. (1999) explain that the boards are not sincere when they provide comparative performance analysis to their shareholders instead they intentionally use the corporate performance of those firms which have not financially performed better.

The practice pertaining to the executive compensation framework and regulatory compliance in the GCC countries has been limited. Everett and Drabich (2010) explain that these countries had no serious commitment to the issues relating to the executive compensation especially before the start of the 2008 global financial crises. However, they acknowledge that the effect of the crises convinced and compelled the related GCC regulatory and monitory bodies to take necessary measures for ensuring the presence and

standard practice of executive compensation, corporate transparency and disclosure requirements[9].

Large number of research studies has focused on the determinants of executive compensation in different research contexts and settings. For example, Fung et al. (2001) studied the relationship between executive compensation and firm performance, and found a strong relationship between the two variables. Schipani and Liu (2002) examined the impact of board characteristics on firm performance and executive compensation in Chinese companies and reported a strong correlation. Study by Core et al. (1999) focused on the effect of board composition on executive compensation. Relation between compensation committee and executive compensation has been the subject of study by Vafeas (2003). Carothers (2004) examined the association between executive salaries and the number of years of service of the CEO.

This study is motivated by the mixed results obtained in the above-mentioned and many other previous studies. Furthermore, there are limited number of studies (e.g. Joshi and Wakil, 2004; Baydoun et al. 2013; Al-Saidi and Al-Shammari, 2013; Abraham, 2013) that have focused on GCC countries on the determinants of executive compensation. The main reason behind the absence was mainly contributed by the fact that limited research has been carried out for highlighting the current situation, type and level of the executive compensation which is being provided to the executives in the GCC region. The objective of this study is to explore the determinants of the executive compensation in the GCC countries. The research examined a sample of 349 listed firms located in five GCC countries (Kuwait, Oman, Qatar, Saudi Arabia and United Arab Emirates) within a time period between 2006 and 2011 by looking at the compensation paid to the top five executives within these companies. In particular, the focus of the research was to explore how total compensation and its components as behaviour (salary) and outcome (bonus) oriented are shaped by firm characteristics, ownership structure, and other corporate governance mechanisms. Additionally, the research also examined the determinants of the choice of compensation type (namely behaviour versus outcome) by the GCC firms.

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[9] In this regard, Baydoun et al. (2013) highlight that Oman was the leading country within the GCC region for offering and providing effective executive reward systems to the top executives, followed by Kuwait and UAE Oman and Kuwait have put in place effective and transparent executive compensation requirements and disclosures.

The research finds that in the GCC countries larger firms and firms with potential future growth pay higher total compensation to their executives. Concentrated ownership structure leads to lower compensation levels while firms with high family ownership tend to pay higher compensation. There is also evidence that external ownership leads to higher total compensation. In terms of behaviour-oriented compensation (i.e. salary), it is found that larger firms and firms with higher leverage pay higher salaries to executives. Firms that have a chairman from the family and have higher presence of executive members in the board tend to pay lower salaries. The findings of the research indicate that managerial as well as institutional ownership of companies tends to lead to higher salaries. In terms of outcome-oriented compensation (i.e. bonus), the study finds evidence that companies that have more growth potential pay higher bonuses. A family related chairman and higher number of executive members in the board is related positively to bonus payments. There is also evidence that ownership by managers and by family results in higher levels of outcome-oriented compensation. It is found that the choice between behaviour versus outcome oriented compensation is mainly influenced by firm size, the presence of executive members on the board, and managerial ownership. Larger companies prefer to pay bonus as part of executive compensation. Companies that have higher number of executives or owned by managers are also tend to pay more compensation through bonuses.

This paper is structured as follows. Next section reviews the literature on the determinants of executive compensation from around the world and from the GCC countries. It also gives background on the GCC countries practices. This section is divided to four sub-sections and provides the definition of executive compensation and its uses as presented in the previous literature, a review of the previous research findings and empirical studies on the determinants of executive compensation, and review of the literature on executive compensation in some of the GCC countries. Section 4.3 explains the methodology and data. Section 4.4 presents the results and discussion and Section 4.5 concludes.

4.2 Literature Review

4.2.1 Definition of Executive Compensation and its Uses[10]

Executive compensation represents total benefits received by the top executive directors of a firm. The compensation includes total salary, other financial and non-financial benefits including long term incentive schemes in the shape of share options. Deb (2009) classifies the executive remuneration into different types, which include base compensation, performance-linked compensation, terminal incentives and perquisites. For instance, compensation under the perquisites includes the facility of personal staff, transportation, car parking, paid leaves and club membership.

Outcome-oriented compensation and behaviour-oriented compensation are main types of executive compensation offered to top executives. Outcome-oriented compensation system refers to a rewarding system which is based on performance and it is rewarded in the shape of stock options, gain-sharing, managerial commission and incentives and stock options (Pravin, 2010; Singh, 2007). On the other hand, behaviour-oriented compensation system provides merit based compensation, such as salary. When comparing the results and motivational strengths of both types of compensation, it is observed that the agency theory prefers and provides support to outcome-oriented compensation as this system enables the employees to actively participate and involve in the day to day affairs of company (Pravin, 2010).

Outcome-oriented compensation has not been effectively practiced in the GCC countries. This is mainly caused by the fact the corporate governance mechanism has not been very effective in this region and consequently the GCC firms find it reasonable to continue performing without having any effective corporate governance practices in their internal rewarding systems (Baydoun, Ryan and Willett, 2013).

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[10] In this work, both compensation and remuneration are separately used. Compensation, received by directors, includes all types of non-financial and financial benefits, rewards, incentives, and direct or indirect benefits obtained through providing the executive services to firms, whereas remuneration only includes financial or tangible benefits availed and they include salary, bonus, and cash.

Many GCC countries have drafted and introduced executive compensation measures[11]. Prior to the 2008 global financial crises, the practice of providing reasonable and attractive remuneration and compensation to the top executives was very limited and was not up to the mark (Everett and Drabich, 2010). After 2009, the related agencies and ministries in United Arab Emirates, Saudi Arabia and Bahrain, drafted a number of corporate governance measures including executive compensation and remuneration. For instance, the UAE's Ministry of Economy issued a resolution detailing the requirements and responsibilities for the Nomination and Remuneration Committee.

In Saudi Arabia, Saudi Arabian Monetary Agency (SAMA) published the draft relating to the salaries and other perks of top banking executives (Everett and Drabich, 2010). The SAMA followed the guidelines of the UAE's Ministry of Economy and asked banks to construct a Nomination and Remuneration Committee. This Committee shall conduct review of the executive compensation policy and assist boards by providing recommendations. And in Kuwait, it has been seen that a healthy competition is discouraged as the government has restricted foreign ownership to 49 per cent (Al-Saidi and Al-Shammari, 2013).

In the following parts of the literature review, executive compensation is defined before the types of executive compensation. To evaluate firm performance indicators, firm characteristics are elaborated. It is followed by the board characteristics and the board ownership. Subsequently, the related literature from the developed countries has been included. Then, the review of literature has been carried out in the GCC countries.

4.2.2 Types of Executive Compensation

Executive compensation refers to any set of rewards given to the top ranking executives. Deb (2009) explains that executive compensation represents both short-term and long-term non-financial and financial rewards received by the top executives especially under a contractual and legal framework. Thereby, remuneration and compensation encompass

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[11] In the behavior-oriented mechanism, traditional performance appraisal rating is the most commonly found measure along with skill-based and competency based pay measures (Charles et al., 2001). On the other hand, result-oriented measures encompass for assessing individual performance, encompass productivity, profitability, sales volume, shareholder return (Charles et al., 2001).

share options, salary, bonus, benefits in kind and pension entitlement (Towers, 2001). Deb (2009) has further classified the executive compensation into four broad categories: base compensation, terminal benefits, performance-linked compensation and perquisites. The base compensation includes allowances, salaries, insurance and medical benefits whereas retirement benefits and severance pay are provided under the label of terminal benefits. Bonuses, stock options, incentive payments and deferred compensation plans are offered when compensation is linked with the performance of the directors. Finally, perquisites consist of housing or leasing benefit, personal staff, club membership, transportation, paid leaves and car parking. Through compensation, executives maximise their wealth (Fleming and Schaupp, 2012). As they earn attractive salary, and other incentives both in the shape of behaviour-oriented and outcome-oriented compensation, executives especially working along with the Chief Executive Officers (CEO), become able to retain impressive amount of wealth.

Executive pay[12] receives considerable attention in the United States (Mohan and Ainina, 2012). The top executives, including CEO, are entitled to receive a hefty amount of salaries, bonuses, share options and a range of other perks and incentives. However, it has been contended that the higher executive compensation given to the top executives is not a choice but a corporate compulsion (Mohan and Ainina, 2012). It can be deduced that if the top executive does not receive market-based remuneration and compensation, he or she would be less interested to improve the corporate performance of the firm. Consequently, the shareholders will have to pay the price of firm's under-performance. To avoid this situation, the board attempts to determine an optimal incentive compensation plan (Essid, 2012). In addition to that, it has been contended that executive compensation is higher particularly when the board is comparatively ineffective and weak vis-a-vis (Bebchuk and Fried, 2003). In this statement, it is clearly stipulated that the board becomes ineffective and dysfunctional when it fails to fulfil its corporate responsibilities and consequently, the individual board members exploit this situation of board in their own favour.

The characteristics of optimal incentive compensation plan consist of both executive remuneration and equity based rewards and incentives for directors (Rampling et al.,

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[12] It reflects the total compensation given to the executive directors including salary, stock options, bonus, and other benefits which are received or expected by the top executive directors.

2013). In this regard, Smith and Watts (1992) contend that high-growth companies prefer provide equity-based compensation plans to their top executives and this type of trend has been more common in faster growing firms. However, Kole (1991) has highlighted that high-growth firms use longer intervals for evaluating management performance especially under the incentive plan of stock-based compensation and this practice has been more common in high growth firms than in the low-growth firms.

Aggarwal and Samwick (1999) contend that pay-performance relationship is very complex in today's business environment as executive will be rewarded with higher pay and other incentives if the executives of the other firms in the same industry provide lower returns to their shareholders. Also, Garvey and Milbourn (2003) found little relative performance evaluation for average executive but they did highlight the evidence of relative performance evaluation for younger executives with limited financial wealth. In this regard, Deli (2002) also finds little empirical evidence of relative performance evaluation in the clear compensation structure for the top executives. Similarly, provided or offered compensation has not been able to avoid the occurrence of corporate scandals; consequently, the bankruptcies of numerous firms, including Enron, Lehman Brothers and Northern Rock, have been frequently reported in many developed countries. Munter and Kren (1995) assert that executive compensation is not primarily designed by the shareholders, the real owners of firm, but the executive directors are entrusted to determine and establish the design and type of executive compensation. Also, in the absence of a lucrative compensation and strong control over executive policies and procedures, the directors may be less inclined to serve the corporate objectives of firms instead they prefer to pursue their personal interests at the cost of organisational short term and long-term objectives (Fama and Jensen, 1983).

4.2.3 What determines executive compensation?

Executive compensation may relate to the firm specific characteristics that may depend on the industry or the economy that the firm is operating in. For example, organisational characteristics, firm's size, firm sector, executive's characteristics, executive's qualifications, previous experience, executives' tenure, executives' age, and role duality are some of the important determinants which directly and indirectly influence on the

executive compensation (Ndoro, 2012). According to Jensen and Meckling (1976), the principal-agent model forms the basis to motivate the managers (agents) to work in the best interests of the company in return for adequate initiatives. Findings by Jensen and Meckling (1976) give rise to the application of agency theory to examine the executive compensation. Kim and Nofsinger (2007) report that separation of ownership and control gives rise to agency problems because of information asymmetry between shareholders and managers. This situation is known as the principal-agency conflict. Bebchuk and Fried (2004) argue that the principal-agent setting cannot provide a complete explanation about CEO compensation and they propose an alternate model in which shareholders can raise their voice whenever they consider that executive compensation is excessive. However, Azasu (2012) argues that agency problem occurs when executive directors have a choice between different investment opportunities; and many times they are inclined to serve their personal interest at the cost of the principal's interests (shareholders' interests). Thereby, it can be deduced that the executive directors choose those investment opportunities which serve their personal interests and they can be used to increase their influence to affect the decision-making process of the shareholders.

However, the relationship between firm size and total executive compensation is also important as it directly affect the type and level of executive compensation that is provided to the current and potential executive directors. Within this context, Jensen (1986) contends that financially stable firms (assumed as larger firms) offer attractive emoluments to executive directors while hiring them. On the other hand, small firms, who are comparatively less financially stable, do not offer such type of attractive offers to the executive directors because they have limited financial resources to avail strategic debt and to return back the debt (Pagliery, 2012).

When taking into account firm size and its effect on executive compensation, it can also be highlighted that the larger the firm size, the higher will be business complexity (Reynolds, 2010). In other words, the larger firm size has dark side as well in which the firm becomes in a position to offer attractive executive compensation whereas managing the business complexity makes it harder for directors to ensure continued expected level of operational and financial performance of the firm. Hijazi and Bhatti (2007) found that the firm size has a close association with the job complexity and the ability of the employer to pay in the determination of executive pay levels. Tosi et al. (2000) found that

firm size accounted for more than 40% of the variance in the executive compensation levels.

According to Guest (2009), with an increase in the size of the board, there is likely to be an increase in the CEO pay. Carothers (2004) studied the relationship between executive compensation and the length of service of the executives and found a positive association between the variables. Raheja (2005) argues that optimal board size can be determined by the trade-off between the extra monitoring ability of external directors and the moral hazard problems associated with the external directors. The board size in turn determines the executive compensation levels. Dalton et al. (1999) finds an advantage in having a larger board size as a larger board provides the opportunity for getting collective information and thus leading to higher firm performance. Basu et al. (2007) examined the association between board size and executive compensation to report an insignificant correlation between the two variables.

The board composition is an indicator for executive compensation (Andreas et al., 2010). Monitoring capability, monitoring effort and independence remain the primary characteristics of board (Linck et al., 2008) and both executive and outside directors retain positions of trust within the board (Abugu, 2012). Zhang (2012) asserts that a diverse board may increase strategic decision-making of the board. Within this context, Kang et al. (2007) elaborate that it is the benefit of the diverse board that the management feels that they are closely monitored by the board. Moreover, Bantel (1994) states that the diverse board becomes effective when the board members represent different educational, functional and occupational background; this heterogeneity remains positively linked to the effective monitoring capability and monitoring effort including the delivery of quality solutions. Core et al. (1999) found an inverse relationship between CEO compensation and the percentage of shares owned by the directors. Their findings indicate a significant amount of cross-sectional variation in CEO compensation and that CEOs get greater compensation when the governance structures are less effective. Fung et al. (2001) have shown that firms with a large number of directors are most likely to restrict CEO compensation in the context of Chinese companies. Schipani and Liu (2002) studied the corporate governance in Chinese listed companies and report that executive compensation levels have a direct bearing on the corporate governance and therefore it is necessary to improve the compensation mechanism to achieve sound corporate governance levels.

Kubo (2001) provided evidence to prove the differential effect of corporate governance on the directors' salary and their incentives.

Outside directors (independent directors) are more independent of the top management (Mehran, 1995). Consequently, the board independence is directly attached to the presence of outside directors. It has been contended that considering their independence from the executive management of the firm, the outside directors are in a strong position to effectively perform their fiduciary responsibilities (Daily and Dalton, 1994). On the contrary, the executive directors are more inclined to attach their interests with the personal priorities of management rather than associating them with the overall organisational objectives (Zhang, 2012). Thus, a higher number of outside directors, on the board, can control the opportunistic behaviours of management and can ensure the effective monitoring of the executive management (Fama and Jensen, 1983). However, despite this fact, the executive directors are also more interested to have a lucrative executive compensation as it enables, encourages and motivates them to align their interests with the interests of shareholders. Vefeas (2003) provides evidence to the negative association between proportion of independent directors on the board and the level of executive compensation. Zhu et al. (2009) examined executive compensation in the Chinese listed firms to report a significant influence of a compensation committee in determining the compensation levels.

However, Conyon and Peck (1998) insist that they do not find strong evidence corroborating the relationship between the fees received by the outside (non-executive) directors with the executive compensation given to the executive directors. Similarly, Mace (1986) argues that the selection process of the outside directors primarily considers the title and the prestige of the potential candidates. Consequently, when non-professional parameters are adopted in the selection process of the outside directors, the performance of such outside directors may not be sufficient to ensure the effective monitoring of the management. It has been argued that the board composition is the indicator of the executive compensation (Andreas et al., 2010). Among various duties and responsibilities, the board is also required to have monitoring capability and carry out monitoring effort along with exhibiting independence in their decision-making process.

Ownership and its reflection on the board structure may also influence executive compensation, for example, foreign ownership, family ownership and inside ownership[13] may directly affect the board structure and management of board affairs. Randoy and Goel (2003) explain that the foreign ownership ensures more effective monitoring of the management performance. Moreover, it has also been argued that large foreign institutional investors are better positioned to reduce the cost of capital (Randoy et al., 2001). Also, a lower agency cost is observed when foreign institutional ownership leads the board affairs and takes major strategic decisions (Stulz, 1999). In this regard, it is important to mention that remuneration committee is a sub-committee which is mandated and authorised by the board and through this structure, the board delegate authority to the remuneration committee to develop an attractive executive compensation by keeping in view all the required market-based incentives encompassing both outcome-oriented and behaviour-oriented compensation.

It is argued that family ownership curtails agency costs and improves corporate performance (Mishra et al., 2001). The decreased agency costs and enhanced corporate performance are chiefly contributed by the inbuilt family traits, including trust, family reliance, paternalism and altruism (James, 1999). However, many authors find it difficult to agree with the effectiveness of the family ownership when the operational performance, under the family ownership, is compared with the foreign ownership and other types of board ownership. Gomez-Mejia et al. (2001) assert that the weaker corporate performance has been observed when the boards are run and controlled by family members. As highlighted above, in the traditional corporate practices, remuneration committee, which is constituted by the board, takes decisions pertaining to the executive directors' incentives and other schemes offered to them. In the family structure, executive compensation may not be as effective as board members share more strong relations than just the business relationships.

On the other hand, inside ownership promotes goal congruence and a sense of ownership among employees. Abor and Biekpe (2007) emphasise that under the arrangement of the inside ownership, employees do not feel the sense of alienation and they are not subject to any stronger scrutiny which is normally carried out by the outside directors.

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[13] Inside ownership represents that management owns some shares of the firm and consequently retains a considerable share in the board's decision-making process.

Consequently, the firm performance experiences a steady and stable growth in the short and long term period. However, lack of transparency becomes a major and the biggest cost of inside ownership (Randoy and Goel, 2003). Thereby, in the absence of transparency, the reported financial and operational performance cannot be relied on. Under this kind of arrangement, inside ownership works positively as they own the company, and they fully understand that the higher and improved firm performance will also improve their executive compensation.

4.2.4 Executive Compensation in the United Kingdom and the United States

Principal-agent theory depends on the application of 'arm's length' contracting between managers and shareholders (Bruce et al., 2005). For this purpose, an appropriate level of executive compensation is highly essential for obtaining a better corporate performance (Buck et al., 2003). Within the United Kingdom, the Greenbury Committee drafted and proposed recommendations relating to the executive compensation and corporate performance (Buck et al., 2003). The proposed recommendations urged firms to replace executive share options with conditional executive share options and long term incentive plans (Buck et al., 2003). In other words, the executive compensation must not be provided until certain executive conditions are satisfied by the executive directors. In this regard, Bertrand and Mullainathan (2001) explain that the current trend, which is based on the share price performance, of offering and providing executive compensation has two aspects; it may increase agency cost and provide compensation to the 'lucky' executives. Core et al. (2003) assert that the share price does not only reflect the financial and operational corporate performance of the firm but it also increases when the entire stock market is expanding, highlighting the aggregate market sentiment and trend. Thereby, some managers may not support the use of share price as a performance indicator and they may prefer to resist this benchmark (Hall and Murphy, 2002). Gregg et al. (2005) provide evidence to the asymmetric relationship between executive pay and firm performance. Gunasekaragea and Wilkinson (2002) also provide evidence to the misalignment between firm performance and managerial compensation in the context of New Zealand.

In the United Kingdom, the Cadbury Committee provided a number of recommendations for executive remuneration. The Committee recommended that the total compensation of executive directors including both the highest paid director and the chair should be disclosed; additionally, this disclosure must provide a breakdown of performance-related incentives and the base salary (Girma et al., 2007). Moreover, the Committee also proposed that it should be the function of remuneration committee to determine executive director's pay and the remuneration committee should be composed of non-executive directors (Girma et al., 2007). The Report highly insists that executive directors should not involve in decisions relating to executive remuneration and compensation (The Cadbury Report, 1992). Also, the Committee recommended that for ensuring transparency and accountability, the composition and membership of the remuneration committee should be made public and it should be attached in the annual report[14].

The Committee recommendations considerably affected the UK companies. Ezzamel and Watson (1997) critically analysed the post-Cadbury business environment and found that some companies have started to include the recommendations in their business practices. Dahya et al. (2002) highlight the effect of Cadbury recommendations particularly on the managerial tenure. Subsequently, this change started to put positive effect on the firm performance (Girma et al., 2007). However, it is important to highlight that the Cadbury Report did not specifically support the need for amendment in the level of executive pay instead it insisted that the level of executive pay should be constituted and designed in accordance with the market needs of firm (Girma et al., 2007). Additionally, Main and Johnson (1993) point out that establishing a transparent executive pay and remuneration would positively affect the corporate performance which would reduce the impact of agency conflict. According to Hodgson (1988), the variance in the level of corporate governance at firm level cannot be considered to have any influence on the institutions and hence cannot influence the executive compensation mechanisms to a large extent. However, the usefulness of Cadbury Report can be understood by the fact that its findings are not binding on the firms instead it contained 'comply or explain' term, enabling the

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[14] In the UK's Companies Act 2006, detailed but comprehensive requirements pertaining to the executive directors' compensation have been provided. If the total compensation received by a director is more than the benchmark of £200,000, then the following information becomes obligation and must be incorporated into the disclosures of the financial statements: total remuneration paid to or receivable by the executive directors; the aggregate sum of gains availed by directors on the exercise of share options; the total sum of money paid to or receivable including the net value of assets (excluding share options and money) received or entitled under the long term incentive schemes (ACCA fact sheet, 2013).

firms to use the findings if they find that their corporate interests are served. In other words, firms are not legally bound to comply with the recommendations of the Report instead they can use any excuse to deviate from the recommendations (Jordan, 2012).

In 1995 in the United Kingdom, Greenbury Report also provided some recommendations for the executive remuneration and compensation. For example, companies should link rewards to performance; and they should prepare and disclose executive directors' pension and remuneration entitlements; additionally, the Greenbury Report proposed that it is advisable to review the rules and procedures pertaining to termination pay and directors' rolling contracts (Oxelheim and Wihlborg, 2008). Solomon (2011) argues that the Greenbury Report was seen as reactive in its nature, as it addressed to public issues and sentiments. However, Solomon (2011) also agrees with the narrative that the Greenbury Report gave more focus and clear recommendations on directors' compensation and pay and this report completed the remaining work of the Cadbury Report.

Various strong regulations have been incorporated into the corporate governance practices in the United States. The Sarbanes-Oxley Act of 2002 proposed to tighten the accounting policies and practices and recommended new obligations and restrictions on the senior corporate executives (Girma et al., 2007). In the United States, the design of the executive pay package more supports the interests of the executive directors than the objectives of firms (Buck et al., 2003). In the incentive schemes, the design is not used as ex ante component, but is included ex post when comparative performance analysis is conducted at Annual General Meetings (Buck et al., 2003). Porac et al. (1999) state boards do not give an objective comparison when their performance is reported to the shareholders. Instead they compare their annual performance with the corporate performance of those firms which have not performed well. Consequently, such corporate practices are carried out to portray that the firm has financially and operationally performed better and this performance is the result of the corporate policies and procedures adopted by the executive board members.

In the United Kingdom, the selection process of outside directors fails to meet the expected corporate benchmarks (Gupta et al., 2008). It has been found that less than one-third of firms, operating outside the FTSE-350, employ a nomination committee; the

procedures adopted by the nomination committee fail to satisfy the benchmark of transparency Higgs (2003, as cited in Gupta et al., 2008). Also, it has been found that the Cadbury Committee recommended that the total compensation of executive directors and the chair must be disclosed and this disclosure should encompass a complete breakdown of performance-related incentives along with the base salary. Also, the Committee proposes that the prime objective of remuneration committee should be to determine and design executive director's pay and other incentives; and the non-executive directors should be more than the number of executive directors working in the remuneration committee. Additionally, the Greenbury Report has provided additional guidelines on the issue of executive compensation by clearly emphasising that the firms should link rewards to performance along with disclosing remuneration and pension given to top executive directors. They also highlight the true reality of corporate governance issues and the seriousness of executive directors to the firm related issues, by describing that the board members do not actively participate in board meetings; they do not prepare well for issues and agendas to be discussed in the board meetings and by and large they remain submissive to the CEO (Baydoun et al., 2013).

4.2.5 Empirical Studies and Findings on the Determinants of Executive Compensation

The literature review in the developed countries has highlighted various empirical findings. A large volume of literature has found evidence to prove that the executive compensation can be considered as an effective means of aligning the interests of managers and shareholders (Hall and Liebman, 1998; Kaplan, 2008). First, Aggarwal and Samwick (1999) found that the top executives are highly rewarded with attractive pay and incentives if the top executives of other firms in the same industry provide lower returns. Additionally, the benchmark of relative performance evaluation is widely used for assessing pay-performance relationship in the developed countries. In this regard, Garvey and Milbourn (2003) highlight that only younger executives are assessed as they are not financially sound. Concerning the relative executive compensation structure, the use of relative performance evaluation has been very limited (Deli, 2002). Similarly, Rajgoal et al. (2006) explain that the agency theory recommends the use of indexed executive compensation for decreasing the effect of relative performance evaluation.

Moreover, a higher executive compensation is not a choice but a corporate compulsion (Mohan and Ainina, 2012). This finding reveals that it is a market norm to offer and provide attractive executive compensation to the potential executive. Nonetheless, past research often has reported only weak or even insignificant association between executive compensation and firm performance (Barkema and Gomez-Mejia, 1998).

Some findings reveal that the use of share price as a performance indicator has not been favourably considered by some managers in deciding the executive compensation structures (Hall and Murphy, 2002). Additionally, Buck et al. (2003) found that the composition of executive pay more serves the interests of executives than the objectives of firms and this trend is common in the United States. To support this claim, it was highlighted that the board do not provide fair comparative analysis while comparing their performance with the competitors. In addition, within the United Kingdom, empirical research was carried out for the period between 1994 to 2006 for assessing the relationship between behaviour-oriented compensation and its relationship with the industrial performance; the results highlighted that asymmetric relationship between variables and the sensitivity between pay and the industry performance was higher and simultaneously elasticises were higher for those firms whose share prices were generating lucrative returns (Gregg et al., 2010).

Executive compensation encompasses salary, bonuses and other incentives (Rezaee, 2009). These determinants are key aspects which represent and highlight the level of motivation and performance of directors serving the interests of shareholders. In this endeavour, directors are not only interested to receive compensation in the form of salary, but they are also inclined to expect other benefits and incentives for improving the overall corporate performance of the firm. In this regard, it is important to mention that additional factors, such as incentives, share option schemes and profit-sharing option are some other determinants which are also offered by firms to directors.

Firm characteristics, board characteristics and board ownership, have attracted attention recently as the main empirical determinants of executive compensation (e.g. Linn and Park, 2005; Linck et al., 2008; Zhang, 2012; Brick et al., 2006; Ryan and Wiggins, 2004). In the firm characteristics size is a main determinant. Within the context of larger firm size, the executive directors have leeway to determine and decide some strategic policies

and operational matters in which they are empowered to assess merits and demerits of any future investment option. And after the initial assessment, it is their prerogative whether to opt for investing in the investment opportunity (Slater, 1999). However, the relationship between firm size and total executive compensation is also important as it directly affect the type and level of executive compensation that is provided to the current and potential executive directors. Within this context, Jensen (1986) contends that financially stable firms (assumed as larger firms) offer attractive emoluments to executive directors while hiring them. On the other hand, small firms, who are comparatively less financially stable, do not offer such type of attractive offers to the executive directors because they have limited financial resources to avail strategic debt and to return back the debt (Pagliery, 2012). When taking into account firm size and its effect on executive compensation, it can also be highlighted that the larger the firm size, the higher will be business complexity (Reynolds, 2010). In other words, the larger firm size has dark side as well in which the firm becomes in a position to offer attractive executive compensation whereas managing the business complexity makes it harder for directors to ensure continued expected level of operational and financial performance of the firm. However, outcome of the investment decides whether the directors have alignment of interests with the shareholders. Within this context, it is important to mention that competent executives are hired as they maintain high standards of performance and commitment (Pratt, 1996). Consequently, their result-oriented future investment decisions represent their commitment towards the objectives of shareholders.

In addition, the board characteristics (executive and non-executive directors) have been discussed to highlight the significance of executive compensation. The rationale for choosing this determinant was that the most of the recent surveys, empirical and primary research are being conducted on the actual role and contribution of directors for the firm's governance (e.g. Bantel, 1994; Kang et al., 2007). In other words, both executive and non-executive directors have received prime attention from researchers for their performance (e.g. Abugu, 2012; Mehran, 1995).

Family, institutional, and foreign board ownership are key types of board ownership (Wright et al., 2013). For example, in the GCC, family-owned firms are considered to be more successful than other types of firm ownership. However, recently, more dynamic changes are taking place in the business world and the result of these changes is that

institutional and foreign-owned firms have outshone the family-owned firms particularly in that region (e.g. Arouri et al., 2014). In addition, institutional ownership is largely retained by the insurance and pension funds in various global fund and pension markets. As the insurance is disallowed in the religion of Islam (Htay et al., 2013)[15], it will be very difficult for the institutional investors to penetrate the Middle East market, and it has been observed that the higher the institutional ownership, the lower the executive compensation is provided (Hartzell and Starks, 2003)..

In addition, it has been observed that the type and level of ownership concentration have direct relationship with the offered and availed total executive compensation[16]. For instance, comparison between management controlled firms and non-management-controlled firms with total executive compensation has clearly highlighted their interaction. It has been observed that higher total executive compensation is provided where higher ownership concentration is observed; on the other hand, the lesser total executive compensation is provided by management-controlled firms (Bryan et al., 2000; Fich and Shivdasani, 2005; Schmidt, 1997; Elston and Goldberg, 2003).

Within this context, the recent literature on the behaviour-oriented compensation (i.e. salary) and outcome-oriented compensation (i.e. bonus) has considerably influenced the level and type of executive compensation. For example, Bebchuk and Fried (2003) argue that the behaviour-oriented compensation is not strongly related to managerial profitability; consequently, it does not substantially increase firm performance. On the other hand, outcome-oriented compensation does not only contribute to the firm performance but also reduces the conflicts of interests between shareholders and directors; similarly, it also aligns their corporate objectives and interests (Eisenhardt, 1989).

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[15] In this regard, it is important to mention that the insurance activity in the shape of business has not been supported by the religious teachings. As a result, at the ground level, any insurance firm is not in a position to enter into the GCC market and continue operating in the region.

[16] The ownership concentration refers to a situation in which small number of shareholders own majority of shares of a company (Grant et al., 2011). In this kind of ownership, ordinary and institutional investors can also retain majority shares in small and large firms. Within this background, Grant et al. (2011) further contend that despite the fact that such shareholders are in small numbers, they have strong rights to exercise in the annual general meetings and in the appointment and retirement decisions of executive directors and senior management as well. Based on this information, it can be deduced that as far as the ownership of firms is concerned, the quantity of small shareholders does not matter but the number of shares owned by the small number of shares.

However, despite the fact that many such corporate activities have been carried out to avoid the occurrence of conflict of interest between shareholders and directors, the corporate debacles, fraudulent activities and white collar crimes have been consistently taking place. Within this context, it can also be deduced that the behaviour-oriented compensation was not considered to be sufficient enough to meet the expectations of executive directors and was not strong enough to discourage executives from involving in illegitimate corporate practices. As a result, the need for more attractive compensation mechanism was required to discourage such practices. And it would not be incorrect to say that the outcome-oriented compensation was appropriately highlighted, promoted and introduced to the corporate culture for reducing the misalignment of interests of shareholders and directors and for improving the agency relationship as well (Minter, 2003).

4.2.6 Literature on the GCC Countries

Many GCC countries have implemented a number of corporate governance measures relating to the remuneration and compensation of the top executive directors of the public and private firms. Prior to the start of 2008 global financial crisis, effective executive remuneration and compensation mechanism was almost unfound in the GCC countries (Everett and Drabich, 2010). They further mention that it is the strong impact of the global financial crises that has compelled many countries, including the United Arab Emirates (UAE), the Kingdom of Saudi Arabia and Bahrain, to enhance corporate transparency, disclosures, and other related measures for reducing the existing gaps in their corporate governance mechanisms. However, despite putting enormous amount of concentration and effort, the ground reality is considerably different. For example, PwC (2012) highlights the issues relating to the corporate governance are not a top corporate priority but a lower strategic concern for many GCC firms and related regulators. This report further elaborates that the main governance issues, particularly in GCC family firms, are the conflict management and corporate succession.

Concerning the existing practices and policies pertaining to the executive compensation in the GCC countries, an empirical study by Baydoun et al. (2013) provides a factual reality about the executive compensation. They found that Oman received the highest

scores for managing and providing effective reward systems in the GCC corporate world; it is followed by Kuwait scoring more that the performance score of the UAE; and both Qatar and Bahrain also obtained very lower scores. The lower scores of the UAE, Bahrain and Qatar are chiefly contributed by the insufficient procedures for dealing with governance issues pertaining to the executive compensation and reward systems; only Oman and Kuwait have clearly established requirements pertaining to the executive compensation disclosures. In the following sub-sections, the study looked at the individual GCC countries' executive compensation issues.

4.2.6.1 United Arab Emirates

Determining and phasing in a number of corporate measures relating to the top executive compensation and remuneration, the UAE's Ministry of Economy entailed and issued the Ministerial Resolution No. 518, which details Governance Rules and Corporate Discipline Standards (Everett and Drabich, 2010). Specifically, article 6, (1.b) encompasses the prime responsibilities of the Nomination and Remuneration Committee (NRC). Based on this information, it can be argued that proposed committee is required to play two different roles: nomination of the top executive directors and ascertainment of remuneration and compensation for the top executive directors. This deviates from the standard practices of the corporate governance pertaining to the nomination and remuneration committee as both have separate mandate and work.

Hassan and Halbouni (2013) examine the committees-performance relationship in the UAE. Consequently, they conclude that segregation of roles and duties between executive and non-executive directors has not been developed yet. Adding further elaboration to this situation, McKnight and Weir (2009) explain that the current nomination, remuneration and other committee members have not sufficient related experience; and it is also possible that many committees are undergoing the early stage of development. Consequently, in the absence of any effective mechanisms, such as remuneration committee, nomination committee and other important pillars of corporate governance, the firms will not be able to provide an effective and market-based executive compensation to executives.

Similarly, Union of Arab Banks (2007) conducted corporate governance survey in numerous banks within the GCC countries. The subsequent findings reveal that boards do not have a majority presence of the independent directors. When the independent directors are in minority, the major strategic decision will be considered and taken by the executive directors. Consequently, the ultimate objectives of the corporate governance will be compromised. And subsequently, the compromised objective of corporate governance will be reflected in the policies in which the absence of effective outcome-oriented and behaviour-oriented compensation will further add fuel to the fire of demotivation. Also, Al-Tamimi (2012) conducted interviews on the issue of corporate governance practices and performance of banks in the UAE. Their findings highlight that the majority of the UAE national banks is not satisfied with the existing practices pertaining to directors' remuneration and executive compensation, composition of board of directors and the corporate governance culture. Consequently, the absence of relevant and effective executive compensation is causing demotivation and making ineffective both types of executive compensation provided to the executive working in the UAE.

4.2.6.2 Saudi Arabia

In 2010, SAMA issued rules pertaining to the executive compensation and remuneration of the top banking executives (Everett and Drabich, 2010). Similar to the guidelines of the UAE's Ministry of Economy, the SAMA also proposed almost same corporate procedures by asking banks to form a Nomination and Remuneration Committee consisting of three members; the Committee shall be mandated to review the compensation policy and assess its effectiveness along with providing recommendations to the related boards (Everett and Drabich 2010)[17].

Family-owned firms encounter numerous financial problems in Saudi Arabia (Gavin, 2010). Baydoun et al. (2013) explain that family owned firms face the problems, such as ineffective oversight and scrutiny, insufficient transparency and disclosures and substantial reliance on the personal and family relations. Consequently, many international financial institutions and lenders have been unwilling to extend the credit

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[17] Due to the shortage of relevant data from the GCC countries and only available data was related to the banking and financial institutions. As a result, the banking statistics have been included.

facility to many Saudi firms. It is the impact of the behaviour of the international financial institutions that compelled the Saudi regulatory authorities to take certain measures for developing the confidence of the international financial institutions (Baydoun et al., 2013).

Within this context, the study of Abraham (2013) pertaining to the foreign ownership and bank performance metrics in Saudi Arabia, looks relevant. Abraham (2013) compares the performance metrics of the foreign banks with the domestic banks. Results highlight that the foreign banks outperform the domestic banks in terms of earning assets, higher leverage and lower allocation to tier I capital. On the other hand, the domestic banks exhibited substantial performance in terms of market valuation (Tobin's Q) and ROA. However, the foreign banks were able to show better corporate performance. Consequently, it can be deduced that the domestic banks do not prefer to use the guidelines pertaining to the corporate governance that are essential for developing and retaining effective corporate firm performance. In addition, it can also be extracted that the foreign ownership improves corporate governance practices as the foreigners have better understanding regarding corporate governance issues.

4.2.6.3 Kuwait

The majority of Kuwait's domestic banks is owned and controlled by individual (families), governmental and institutional shareholders (Al-Saidi and Al-Shammari, 2013)[18]. They contend that the banking industry lacks healthy competition as the regulators have constrained foreign ownership to 49 per cent. In addition, they also mention that the Company law does not discourage appointing the same person as CEO and board chairman; similarly, the law has not provided any guidelines pertaining to setting up a remuneration committee or any other committee. In the absence of any regulatory mechanism, the public and private firms are on their will whether to have or not to have remuneration committee determining executive remuneration and compensation for the executive directors.

4.2.6.4 Bahrain

In 2010, the Bahrain Ministry of Industry and Commerce established and issued corporate governance code comprising of nine fundamental principles of corporate governance practices of international standards; the Principle 5, which entails the Remuneration Committee, states that the Board of Directors shall set up a Remuneration Committee consisting of at least three members (Everett and Drabich 2010). Joshi and Wakil (2004) point out that the dearth of non-executive directors remains a primary issue for countries like Bahrain. Moreover, they also state that it is comparatively difficult to find genuinely independent non-executive directors; this shortage is prevalent throughout the GCC countries including the UAE (Baydoun et al., 2013).

4.2.7 Empirical Findings for the GCC Countries

The GCC countries have different priorities. In a recent report of PwC (2012), it has been highlighted that the corporate governance issues are not a top priority for firms working

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[18] Due to the unavailability of required studies pertaining to the non-financial institutions, the study used the financial institutions to complete the literature review part.

in the Middle East instead they are more inclined to address the problems of corporate succession and conflict management. In this regard, it is important to mention that the firms in the Middle East are mainly facing this problem because little research on the corporate performance in the Middle East countries has been conducted so far. Consequently, the firm performance will not be appropriately highlighted and represented by the any piece of field research and the extent of this impact can be deduced from the fact that before 2008 financial crises, there was no comprehensive structure for executive compensation in the Middle East (Everett and Drabich, 2010).

The literature on the GCC countries for the executive compensation is very limited. Certainly, the executive compensation mechanism is in its early stage of development and also, the literature on the GCC is mostly based on individual countries and on banking industry (such as Arouri et al., 2014). Consequently, their findings only explain and justify the corporate governance issues relating to the banking industry and other papers are also limited only to different types of ownership and executive compensation.

Baydoun et al. (2013) look at providing some understanding about the reward systems in the GCC countries. However, their research has limitations. The data (the secondary data from the OECD survey conducted in 2005) is outdated. Hence, the findings are only applicable to the reward systems which were functional before the 2008 financial crises. In this regard, Stubing (2014) does not disagree that the GCC corporate climate has considerably evolved and changed especially after the severe effects of the 2008 global financial crises (Stubing, 2014).

The findings of this contribute to the research gap on GCC countries determinants of executive compensation in twofold. Firstly, the sample used in the study of covers almost entire GCC region, excluding Bahrain. Currently, no previous research has been available for the current topic and the inclusion and publication of this research will enable the current and potential researchers, market analysts, current and potential investors, both institutional and non-institutional, will be in a position to understand the current trend relating to the determinants of executive compensation in the GCC countries.

Secondly, unlike other studies on the GCC, this study focuses on non-financial firms from a variety of sectors, including industrial, real estate, food and beverages, services industry,

utilities, transport and telecommunication. This research will enable the different stakeholders to understand the current executive compensation practices and the involvement of different determinants for the executive compensation. Through this understanding, they will be in a better position to take more informed decisions.

4.2.8 Employment and Incentives – A View from Labour Economics/Personnel Economics

Corporate governance is concerned with the relationship between three different sets of stakeholders – capital, management and employees. The core of corporate governance deals with the actions of the people who owns and controls the firm, people in whose interest the firm is governed and the direct and indirect ways in which control could be exercised in order to maximise the objectives of the firm (Blanpain, 2011). In this context, managing labour can be considered one of the important elements. Employee relations from a governance perspective can be studied by using the developments in the field of personnel economics. Research on personnel economics as a branch of labour economics has focused on incentives and compensation among other things and the contributions from such research help managers to take meaningful decisions that help in running the businesses more efficiently (Lazear, 1998). Encouraging employees to put in their best efforts is the central aim of the study of personnel economics. In a situation, where the efforts of the employees are not contractible it is possible to derive the socially efficient level of worker effort by paying the worker for the full value of output that can be obtained from the employees.

From a governance perspective, it is critical that the labour market conditions are analysed thoroughly so that firms can devise their employment and incentive policies in such a way to maximise their profits. However, it has to be understood that both demand and supply side of labour market is affected by information asymmetries. On the demand side, it is for the firms to establish processes and structures to reduce the uncertainty about the availability of suitable employees. This is because the firms have only limited information about the prospective candidates that might suit the jobs available with the firm (Blanpain, 2011). In order to overcome the issues connected with information asymmetry in this respect, firms devise selection process that precede (like written tests, personal

interviews, checking the credentials) and processes that follow the hiring (like probation period and in-house training). From the supply side, prospective employees also do not have complete information about the jobs which they are going to perform before and even after they are hired. Such information asymmetries may create a situation in which the firm ends up hiring undesirable candidates or candidates that may not fit into the positions for which they were hired (Shapiro and Stiglitz, 1984).

Therefore, selection processes are designed to prevent the hiring of unsuitable candidates. If there are information asymmetries after the hiring process is completed, such a situation might lead to agency problems resulting in moral hazard. The agency problem can arise because of two related factors. First is the presence of divergent interests between the owner (principal) and the employee (agent); the second factor is the difficulties involved in observing the behaviour of managers being the agents of the owners. When these two situations are present, there is the likelihood that the behaviour of the managers (agents) may diverge from achieving the established goals of the firm (Blanpain, 2011). According to economic theory, agents' behaviour can be redirected towards achieving the goals of the firm by creating incentives so that the managers remain compensated for putting their efforts in achieving the firms' goals. Firms may also consider institution of performance appraisal systems and performance-linked pay systems to overcome the agency problems. Again, from a good corporate governance point of view, operational solutions like creation of explicit or implicit contracts with managers may be considered as an optimal solution. There again firms have to deal with the dilemma of balancing short-run incentives against the long-run outcomes expected out of such incentives.

The balance of control between shareholders and managers signifying the strength of corporate governance determines the degree of agency cost within a firm. With the balance of control lying more in favour of shareholders, firms devise incentive schemes for managers so that the managers focus on wealth-maximising activities for and on behalf of the shareholders. Contrastingly, if the managers appear to have more control, they may have greater discretion to involve in activities resulting in personal gains to them (managers). Therefore, the optimal contracting hypothesis suggests that board of directors as agents loyal to shareholders are interested in minimising agency costs with a view to maximising shareholders' wealth by increasing the firm value (Grossman and Hart, 1983). The board of directors strives to achieve this by actively monitoring the

managers and other executives and by assigning incentives and responsibility in an optimal way. However, as suggested by managerial power hypothesis, board of directors do not always deal with all fairness in the matter of executive incentives, especially when the board is not independent from the management and the members of the board are more close to the executives of the firm (Bebchuk et al. 2002). Social network theory, on the other hand, suggests that board members tend to strengthen their social ties with management with increase in their tenure as members of the board (Harris and Helfat, 2007).

Thus, according to neoclassical view, executive incentives offer a solution to mitigate the principal-agent problem that arises between owners that are risk-neutral and managers that are risk-averse. In this context, pay for performance may be a trade-off between the necessity to incentivise the managers and the option to insure them against idiosyncratic risk (Holmstrom, 1979). On the basis of this proposition, firms may choose suitable compensation packages which may be decided on the basis of degree of risk-aversion among the managers and the incentives to be offered to them. From a corporate governance perspective, it is important that there is an efficient matching between managerial skills and specific characteristics of the firm. Another economic view is the managerial rent extraction.

The phenomenon of managerial rent extraction associates executive incentives to the ability of the managers to extract rents. This view suggests that where there is weak corporate governance exists the managers will find opportunities to skim profits from the firm which would lead to a higher level of executive compensation (Bebchuk and Fried, 2004). The efficiency in matching the managerial skills and firm characteristics leads to a situation, where the executive compensation depends on the ability of managers to produce a multiplicative effect on firm performance. Here, the executive compensation is likely to be fixed on the basis of the ability of the managers to increase the productivity and therefore, better managers will be fitted in large firms (Tervio, 2008). Optimal incentive contracts can be created where there is low ownership concentration and its negative correlation with size of the firm (Edmans et al. 2009). Similarly when firms differ in terms of degree of risks they face or in their ability to use the managerial skills, inefficient incentive contracts and allocation of managers across firms is bound to happen. Thus, governance failures lead to negative externalities from a contracting standpoint

which might justify the need for regulations governing executive incentives (Hermalin and Weisbach, 2006).

4.2.9 Methodology and Data

4.2.9.1 Empirical Model

We contribute to the above mentioned literature on determinants of executive compensation in the GCC countries. A number of previous studies focusing on the determinants has used econometric models incorporating different dependent and independent variables. Following earlier literature such as Mehran, 1995; Core et al., 1999; Buck et al., 2003; Basu et al., 2007; Graham and Qiu, 2008; Guest, 2009; Andreas et al., 2010, this study investigated this link using four alternative dependent variables, namely total executive compensation, the amount of total salaries, the amount of total bonuses and finally, the ratio of bonuses to total executive compensation.

We run our analysis using pooled OLS regressions. OLS regression model has been of great use in examining the impact of a number of explanatory variables on executive compensation in large number of previous studies (e.g. Mehran, 1995; Chung and Pruitt, 1996; Core et al., 1999; Graham and Qiu, 2008; Abed et al., 2014).

Endogeneity in the context of econometrics refers to the correlation between one of more explanatory variables and the error term which are part of an econometric model. There are a number of situations in which endogeneity may arise in the study of relationship among variables. For example, the effect of an omitted explanatory variable may cause endogeneity. Measurement error in an explanatory variable adopted for the study, the presence of a causal loop between the independent and dependent variables and omitting fixed effects are some of other instances which might lead to endogeneity issues (Antonakis et al. 2014). Empirical research on corporate finance-related issues might have serious impact of endogeneity because of the difficulty in finding the endogenous factors with which the relations that are being examined can be identified. According to Roberts and Whited (2011), although many empirical research studies suggest that improved

performance can result from the presence of certain governance structures, the fact that these research studies are affected by endogeneity issues cannot be ignored. Presence of endogeneity issues has serious implications on the usefulness of the findings from the empirical studies if such issues are not dealt with properly. Endogeneity has been found to present serious issues affecting the findings of research studies focusing on the relationship between corporate governance and firm performance because many governance and performance variables are most likely to possess endogenous characteristics (Dalton et al. 1999).

Unobservable heterogeneity and simultaneity have been found to be the two potential sources of endogeneity that could affect empirical studies relating to corporate governance research (Wintoki et al. 2012). The possibility of past firm performance affecting the current values of governance variables is another source of endogeneity. Borsch and Koke (2002) found a most common problem of the presence of endogeneity in certain variables adopted by research studies on corporate governance. In fact, Borsch and Koke (2002) found reverse causality in the relationship between corporate governance and firm performance. Study by Lehn et al. (2009) on the determinants of board size and composition found significant impact of firm size, growth opportunities and geographical distribution to endogenously affect the board size and composition.

Pathan and Skully (2010) studied the board structure in the context of banking companies and found that size of the banks had a significant impact on the number of members in the board. The study used several measures like the use of lagged values of the explanatory variables as instrumental variables and adoption of three-stage least squares to avoid the effect of endogeneity issues on the research findings. On the other hand, Wintoki et al. (2012) used a dynamic panel generalised method of moments (GMM) estimator to deal with endogeneity concerns in their study on the effect of board structure on firm performance and the determinants of board structure which are two important aspects of any corporate governance study. Wintoki et al. (2012) caution that ignoring the dynamic nature of the relationship between board structure and corporate performance in empirical studies might lead to significant issues. According to Wintoki et al. (2012), the unobserved heterogeneity and simultaneity are addressed by the valid and powerful tools provided by the GMM estimator which incorporates the dynamic characteristics of internal governance mechanisms. Himmelberg et al. (1999) found that exogenous

changes in the contracting environment of a firm are likely to endogenously determine the managerial ownership and performance of the firm.

In the econometric model developed for the current research, there is the likelihood that the model might suffer from the impact of endogeneity issues, because of the presence of a reverse causality between firm performance and the governance structures adopted as explanatory variables for the study. There is also a possibility that some unobservable factors affect the firm performance. Similarly, the executive compensation structure may also be subject to the influence of past performance of the firm which factor has not been taken into account while developing the econometric model. However, undertaking a system of simultaneous equations and adopting a two-stages least squares (2SLS) regression may, to some extent, alleviate the endogeneity effects on the results.

The empirical models used to examine the key determinants of executive compensation in GCC countries. First we start by looking at the total executive compensation (in the form of salary and bonus) paid to top five executive directors as a dependent variable. This model is given below:

$$Total\ executive\ ompensation_{i,t} = \beta_0 + \beta_1 Concentrated\ Ownership_{i,t}$$

$$+ \beta_2 Managerial\ Ownership_{i,t} + \beta_3 Institutional\ investor\ Ownership_{i,t}$$

$$+ \beta_4 Family\ Ownership_{i,t} + \beta_5 Foreign\ Ownership_{i,t}$$

$$+ \beta_6 Government\ Ownership_{i,t} + \beta_7 External\ Ownership_{i,t}$$

$$+ \beta_8 Board\ Size_{i,t} + \beta_9 Chairman\ family_{i,t}$$

$$+ \beta_{10} Independent\ Directorss_{i,t} + \beta_{11} Executive\ Directors_{i,t}$$

$$+ \beta_{12} Firm\ Size_{i,t} + \beta_{13} Leverage_{i,t} + \beta_{14} Market\ to\ book_{i,t}$$

$$+ \beta_{15} Return\ on\ assets_{i,t} + \sum_{y=1}^{Y-1} \beta_y \times Year_{i,y} + \sum_{j=1}^{J-1} \beta_j \times Industry_{i,j}$$

$$+ \sum_{c=1}^{C-1} \beta_c \times Country_{i,c} + e_{i,t,y,j,c}$$

In the second stage of our analysis we separate the total executive compensation to its components. We then look at the amount of total salary paid to top five executive directors as separate dependent variable to capture the determinants of behaviour oriented. This model is given below:

$$
\begin{aligned}
Salary_{i,t} = \ & \beta_0 + \beta_1 Concentrated\ Ownership_{i,t} + \beta_2 Managerial\ Ownership_{i,t} \\
& + \beta_3 Institutional\ investor\ Ownership_{i,t} + \beta_4 Family\ Ownership_{i,t} \\
& + \beta_5 Foreign\ Ownership_{i,t} + \beta_6 Government\ Ownership_{i,t} \\
& + \beta_7 External\ Ownership_{i,t} + \beta_8 Board\ Size_{i,t} \\
& + \beta_9 Chairman\ family_{i,t} + \beta_{10} Independent\ Directorss_{i,t} \\
& + \beta_{11} Executive\ Directors_{i,t} + \beta_{12} Firm\ Size_{i,t} + \beta_{13} Leverage_{i,t} \\
& + \beta_{14} Market\ to\ book_{i,t} + \beta_{15} Return\ on\ assets_{i,t} + \sum_{y=1}^{Y-1} \beta_y \times Year_{i,y} \\
& + \sum_{j=1}^{J-1} \beta_j \times Industry_{i,j} + \sum_{c=1}^{C-1} \beta_c \times Country_{i,c} + e_{i,t,y,j,c}
\end{aligned}
$$

We also look at the amount of total bonuses paid to top five executive directors as separate dependent variable to capture the determinants of outcome oriented compensation. This model is given below:

$$
\begin{aligned}
Bonus_{i,t} = \ & \beta_0 + \beta_1 Concentrated\ Ownership_{i,t} + \beta_2 Managerial\ Ownership_{i,t} \\
& + \beta_3 Institutional\ investor\ Ownership_{i,t} + \beta_4 Family\ Ownership_{i,t} \\
& + \beta_5 Foreign\ Ownership_{i,t} + \beta_6 Government\ Ownership_{i,t} \\
& + \beta_7 External\ Ownership_{i,t} + \beta_8 Board\ Size_{i,t} \\
& + \beta_9 Chairman\ family_{i,t} + \beta_{10} Independent\ Directorss_{i,t} \\
& + \beta_{11} Executive\ Directors_{i,t} + \beta_{12} Firm\ Size_{i,t} + \beta_{13} Leverage_{i,t} \\
& + \beta_{14} Market\ to\ book_{i,t} + \beta_{15} Return\ on\ assets_{i,t} + \sum_{y=1}^{Y-1} \beta_y \times Year_{i,y} \\
& + \sum_{j=1}^{J-1} \beta_j \times Industry_{i,j} + \sum_{c=1}^{C-1} \beta_c \times Country_{i,c} + e_{i,t,y,j,c}
\end{aligned}
$$

Finally, the ratio of bonuses to total executive compensation is used to gauge the choice between the two types of compensation. This model is given below:

$$
\begin{aligned}
Bonus\ to\ total\ executive\ compensation_{i,t} =\ & \beta_0 + \beta_1 Concentrated\ Ownership_{i,t} \\
& + \beta_2 Managerial\ Ownership_{i,t} + \beta_3 Institutional\ investor\ Ownership_{i,t} \\
& + \beta_4 Family\ Ownership_{i,t} + \beta_5 Foreign\ Ownership_{i,t} \\
& + \beta_6 Government\ Ownership_{i,t} + \beta_7 External\ Ownership_{i,t} \\
& + \beta_8 Board\ Size_{i,t} + \beta_9 Chairman\ family_{i,t} + \beta_{10} Independent\ Directorss_{i,t} \\
& + \beta_{11} Executive\ Directors_{i,t} + \beta_{12} Firm\ Size_{i,t} + \beta_{13} Leverage_{i,t} \\
& + \beta_{14} Market\ to\ book_{i,t} + \beta_{15} Return\ on\ assets_{i,t} + \sum_{y=1}^{Y-1} \beta_y \times Year_{i,y} \\
& + \sum_{j=1}^{J-1} \beta_j \times Industry_{i,j} + \sum_{c=1}^{C-1} \beta_c \times Country_{i,c} + e_{i,t,y,j,c}
\end{aligned}
$$

Independent variables are drawn from firm characteristics, corporate performance, board characteristics and ownership structure. Table 4.1 presents the definitions of all variables used for each category. There are fifteen independent variables in this study, divided into three groups. The first group is board characteristics which includes board size, chairman family, independent directors and executive directors. The second group is financial characteristics including firm size, leverage, market to book and return on assets. The last group is ownership structures which include concentrated ownership, managerial ownership, institutional investor ownership, family ownership, foreign ownership, government ownership and external ownership.

4.2.9.2 Data and Sources

Our sample includes 349 listed firms from 2006 to 2011 from five GCC member countries, namely Kuwait, Oman, Qatar, Saudi Arabia and United Arab Emirates. Financial firms, such as banks and insurance companies, are excluded from this study due to the unique nature of the sector.

Data is collected through a combination of resources as Thomson one banker, Thomson.com, Datastream and annual reports. All of the board characteristics and compensation structure data used in this study were manually collected from the annual reports for all firms. The financial data used in this study was obtained directly from Datastream. The ownership structure data was collected from Thomson.com. However, it is important to mention that there are limitations to the data collection, in particular in relation to the distribution of salary and bonuses. In our sample 349 firms report the level of total compensation they give to their top five executives. However, only 167 of these include the distribution of salary and bonuses within the total compensation. Also, some of annual reports are missing during the period of the study.

Table 4.1 Definitions of dependent and independent variables

This table reports the definition of the variables that are used in the study. For ownership variables we do not report the values if shares owned is less than 5 per cent. All the variables are measured at the end of each year. Compensation figures are reported in US Dollars. Sources: Thomson one.com, Datastream and annual reports of the companies.

Compensation Structure

Total Executive Compensation	The annual cash compensation paid to top five executive directors in terms of salary and bonuses. Log of the variable is used
Salaries	The annual salary paid to top five executive directors. Log of the variable is used
Bonuses	The annual bonuses paid to top five executive directors. Log of the variable is used
Bonus to total compensation	The percentage of bonuses to total executive compensation

Board Characteristics

Board size	The total number of directors on the board. Log of the variable is used
Executive directors	The number of executive directors divided by the board size
Independent directors	The number of independent directors divided by the board size
Chairman family	Equals to 1 if the chairman is a member of the family owning the company and 0 otherwise

Ownership Structure

Managerial ownership	The percentage of shares owned by managerial (CEO and chairman) for shareholding of 5 per cent or more
Institutional investor ownership	The percentage of shares owned by corporation, investment manager, investment funds and government for shareholding of 5 per cent or more
Family ownership	The percentage of shares owned by family for shareholding of 5 per cent or more
Government ownership	The percentage of shares owned by local government for shareholding of 5 per cent or more
Foreign ownership	Is a dummy variable taking the value of 1 if foreign investors owned shares in the company and 0 otherwise
External ownership	The percentage of shares owned by outsiders. It equals to total ownership minus the total of managerial and family ownership for shareholding of 5 per cent or more
Concentrated ownership	The log of Herfindahl Index for measuring concentrated ownership. The Herfindahl index is defined as the sum of the squared sums of all owners shareholdings

Financial and economic characteristics

Return on assets (ROA)	The ratio of net income to total assets
Leverage	The ratio of total debt to total liabilities
Firm size	The natural logarithm of total assets
Market to book	Market to book multiple of the firm's equity
Industry dummy variables	Each dummy variable equals to 1 for the specific industry reported and 0 otherwise. The industry classifications are Industrial, Services, Real estate and Building, Food and Beverage, Transport, Telecommunication and Utilities
Year dummy variables	Each dummy variable equals to 1 for the specific year variables (2006 to 2011) are reported and 0 otherwise
Country dummy variables	Each dummy variables equals to 1 for the specific country reported and 0 otherwise. The countries are Kuwait, Oman, Qatar, Saudi Arabia and United Arab Emirates

4.3 Results and Discussion

4.3.1 Descriptive Statistics

The descriptive statistics of the variables used in the study is presented in Table 4.2. The average executive compensation paid to top five executive directors in total in the GCC region is USD 2,078,261 throughout this period. In the absence of a comprehensive comparable data on executive compensation from OECD or other Western countries, it becomes undeterminable whether the level of executive compensation in the GCC countries is in line with or more than that of other countries. However, it is important to mention that the GCC firms are generally smaller than firms operating in the developed countries, and consequently it can be inferred that the CEOs of companies operating in the GCC countries might receive lesser amount of compensation as compared to their counterparts in the developed countries.

Similarly, when bonuses are taken into account, the average value is USD 598,143. Based on the average salary (USD 1,169,695) and bonus, it can be highlighted that the GCC firms prefer and use salaries more for executive compensation. The average board size is 7.27 members for the sample in the GCC countries. As for the firm characteristics, the table highlights that on average firm size is USD 5.45 million and a relatively low standard deviation of 5.41 which again demonstrates that most of the GCC firms are smaller. The correlation matrix for all variables used in the study is presented in Table 4.3.

4.3.2 Results of the Regression Analysis

4.3.2.1 Determinants of Total Executive Compensation

We present our results for total executive compensation in Table 4.4 in six models by introducing variables gradually and using alternative variables separately. Looking at firm characteristics first, it is found, in the majority of models, a positive and statistically

significant relationship between firm size and total executive compensation. Similar results have been provided the findings of Jensen (1986) who contends that large firms offer more attractive executive compensation. Similarly, the study reports a

Table 4.2 Descriptive statistics

This table reports descriptive statistics of the variables that are used in the study. For ownership variables we do not report the values if shares owned is less than 5 per cent. All the variables are measured at the end of each year. Sources: Thomson one.com, Datastream and annual reports of the companies. Definitions for all the variables are provided in Table 4.1.

Variable	Number of observations	Mean	Median	Std. Dev	Minimum	Maximum
Compensation Structure						
Total Executive Compensation	1523	2,078,261	6,651,991	806,432	3,683	126,000,000
Salaries	538	1,169,695	5,181,242	610,983	634	116,000,000
Bonuses	538	598,143	1,483,838	203,631	0.00	15,500,000
Bonus to total compensation	538	0.30	0.22	0.28	0.00	1.00
Financial and economic characteristics						
Firm size	1523	5.45	1.78	5.41	0.61	11.39
Leverage	1523	0.23	0.20	0.19	0.00	0.89
Market to book	1523	3.14	3.54	2.00	0.00	32.18
Return on assets (ROA)	1523	0.07	0.10	0.07	-0.45	0.47
Ownership Structure						
Concentrated ownership	939	6.27	1.37	6.27	1.75	9.21
Managerial ownership	939	0.04	0.10	0.00	0.00	0.95
Institutional investor ownership	939	0.34	0.26	0.31	0.00	1.00
Foreign ownership	939	0.28	0.45	0.00	0.00	1.00
Family ownership	939	0.05	0.14	0.00	0.00	0.85
Government ownership	939	0.06	0.15	0.00	0.00	0.81
External ownership	939	0.45	0.24	0.45	0.02	1.00
Board Characteristics						
Board size	1523	7.27	1.89	7.00	3.00	13.00
Chairman family	1523	0.38	0.48	0.00	0.00	1.00
Independent directors	1523	0.78	0.25	0.86	0.00	1.00
Executive directors	1523	0.11	0.11	0.11	0.00	0.71

consistent and statistically significant relationship between market to book value and executive compensation.

In addition, it has been observed that larger firm size, among other factors, increases business complexity (Reynolds, 2010)[19]. In this regard, it is important to mention that this aspect is considerably existing in the real business structures because the larger firm sizes

---

[19] Transnational firms have complex business structure in which entire business set up is differently established. Additionally, unique chain of command and structure, local, national, regional and international presence of offices and supply chains and operational and strategic strategies increase complexity to the business activities.

experience substantial level of complexity in which it is very difficult for the firms to control all direct and indirect factors that influence on the smooth functioning of the firm.

Table 4.3 Correlation matrix

This table reports the correlation matrix for the variables that are used in the study. For ownership variables we do not report the values if shares owned is less than 5 per cent. All the variables are measured at the end of each year. Sources: Thomson one.com, Datastream and annual reports of the companies. Definitions for all the variables are provided in Table 4.1.

	Total Executive Compensation	Salaries	Bonuses	Bonus to total compensation	Firm size	Leverage	Market to book	Return on assets (ROA)	Concentrated ownership	Managerial ownership	Institutional investor ownership	Foreign ownership	Family ownership	Government ownership	External ownership	Board size	Chairman family	Independent directors	Executive directors
Total Executive Compensation	1.00																		
Salaries	0.77	1.00																	
Bonuses	0.76	0.16	1.00																
Bonus to total compensation	0.34	-0.08	0.60	1.00															
Firm size	0.46	0.33	0.37	0.30	1.00														
Leverage	0.14	0.18	0.03	-0.05	0.27	1.00													
Market to book	0.00	0.11	-0.13	-0.24	-0.31	0.13	1.00												
Return on assets (ROA)	-0.10	-0.10	-0.06	0.02	-0.07	0.05	0.03	1.00											
Concentrated ownership	-0.11	-0.07	-0.09	-0.07	0.08	0.11	0.20	-0.01	1.00										
Managerial ownership	0.05	0.03	0.07	0.18	0.02	0.01	-0.12	-0.01	0.10	1.00									
Institutional investor ownership	-0.01	0.01	-0.03	-0.11	0.18	0.19	0.28	-0.03	0.73	-0.27	1.00								
Foreign ownership	0.21	0.17	0.16	0.12	0.38	-0.03	-0.08	-0.06	0.16	-0.26	0.24	1.00							
Family ownership	-0.01	0.01	0.00	0.00	-0.15	0.08	-0.03	0.04	0.02	0.36	-0.17	-0.22	1.00						
Government ownership	0.11	0.03	0.13	0.08	0.33	-0.06	-0.02	-0.05	0.42	-0.19	0.45	0.65	-0.17	1.00					
External ownership	-0.06	-0.06	-0.02	0.02	0.10	0.22	0.15	-0.03	0.77	0.19	0.67	0.08	0.26	0.28	1.00				
Board size	0.20	0.09	0.22	0.28	0.40	-0.09	-0.34	-0.02	-0.19	0.01	-0.14	0.32	-0.19	0.10	-0.13	1.00			
Chairman family	-0.04	-0.07	0.02	0.03	-0.16	-0.07	0.02	0.03	-0.08	0.31	-0.20	-0.29	0.34	-0.23	0.09	-0.01	1.00		
Independent directors	-0.02	0.03	-0.08	-0.30	-0.35	-0.02	0.45	-0.08	0.01	-0.21	0.12	-0.12	-0.13	-0.10	-0.07	-0.30	-0.06	1.00	
Executive directors	0.11	0.06	0.12	0.22	0.26	0.03	-0.22	0.00	-0.11	0.34	-0.20	-0.01	0.19	-0.17	-0.01	0.10	0.12	-0.43	1.00

Table 4.4 Determinants of total executive compensation

This table presents coefficient estimates for pooled OLS regressions estimating the relationship between corporate governance variables and performance. Industry, year and country dummy variables control for the macroeconomic conditions. Robust standard errors are reported in parenthesis. ***, ** and * represents significance levels at 1%, 5% and 10%, respectively. Definitions for all the variables are provided in Table 4.1.

	Model 1	Model 2	Model 3	Model 4	Model 5	Model 6
Financial and economic characteristics						
Firm size	0.48***	0.47***	0.45	0.45***	0.46	0.45***
	(0.02)	(0.02)	(0.03)	(0.03)	(0.03)	(0.03)
Leverage	0.10	0.10	0.32*	0.33*	0.26	0.31*
	(0.13)	(0.13)	(0.17)	(0.18)	(0.18)	(0.17)
Market to book	0.03***	0.03***	0.03***	0.03***	0.03***	0.03**
	(0.01)	(0.01)	(0.01)	(0.01)	(0.01)	(0.01)
Return on assets (ROA)	0.24	0.24	0.17	0.17	0.13	0.18
	(0.23)	(0.23)	(0.30)	(0.30)	(0.29)	(0.30)
Board Characteristics						
Board size		0.20	0.32*	0.31*	0.29*	0.29*
		(0.12)	(0.17)	(0.17)	(0.17)	(0.17)
Chairman family		0.09*	-0.09	0.01	-0.01	0.04
		(0.05)	(0.07)	(0.07)	(0.07)	(0.07)
Independent directors		0.12	0.28	0.28	0.25	0.27
		(0.14)	(0.18)	(0.18)	(0.17)	(0.17)
Executive directors		-0.28	0.02	0.03	-0.03	0.16
		(0.23)	(0.34)	(0.34)	(0.34)	(0.33)
Ownership Structure						
Concentrated ownership			-0.08***	-0.08***	-0.04*	-0.10***
			(0.03)	(0.03)	(0.25)	(0.03)
Managerial ownership			0.42	0.46	0.25	
			(0.30)	(0.30)	(0.27)	
Institutional investor ownership			0.15	0.14		
			(0.18)	(0.18)		
Family ownership			0.44**	0.45**	0.39*	
			(0.22)	(0.23)	(0.22)	
Foreign ownership				0.53		
				(0.78)		
Government ownership					0.41	
					(0.29)	
External ownership						0.38*
						(0.18)
Industry dummy variables	Yes	Yes	Yes	Yes	Yes	Yes
Year dummy variables	Yes	Yes	Yes	Yes	Yes	Yes
Country dummy variables	Yes	Yes	Yes	Yes	Yes	Yes
Number of observations	1531	1523	939	939	939	939

Leverage seems to be positively related to the total executive compensation, but the statistical significance is low, and this finding is not valid for all models. Andreas et al. (2010) find a negative relationship between leverage and total executive compensation for directors. They interpret their finding from the point that the role of higher leverage is not positively seen by the directors instead highly leveraged firms are considered to be riskier. If a firm is highly leveraged and pays substantial amount of financial cost, in future, the firm may not be in a position to continue providing the stipulated executive compensation to directors.

The subsequent support to the ascertainment of this hypothesis is also provided by the relationship between leverage and total executive compensation. Normally, it has been seen that smaller firms are less inclined to take more debt because their financial capability and business operations are not appropriately equipped to return back the debt (Pagliery, 2012). Thereby, they have higher tendency for relying on their available financial resources for maintaining their business cost which is completely opposite to the larger firms' capability for using debt facility for pursuing their medium term strategic goals and objectives. In other words, firm size and leverage are two factors highlighting firm's overall executive director's compensation in the GCC countries[20].

Next, the study looked at the ownership structure's impact on total executive compensation. The findings of the research indicate that family ownership has a positive relationship with the total executive compensation. As families have both regulatory (governmental power) and firm ownership, they are in a position to take both strategic and operational decisions. This finding demonstrates that the influence of families for executive decision-making is largely prevalent throughout the GCC firms. Gomez-Mejia et al. (2001) argue that family-controlled firms exhibit weaker corporate performance, reflecting that many fundamental corporate governance benchmarks are compromised when the board is controlled by members of the same family. Moreover, it is interesting to highlight that the firms operating in the GCC countries have not practically experienced the benefits or positive side of corporate governance; instead, they prefer to remain attached with the traditional business ownership structure in which one or a few board

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[20] When the size and scale of GCC firms are compared with the firms operating in the UK and the US, it can be deduced that the GCC firms are comparatively smaller business scale and business operations as well.

members have full and unchallenged power to make and revoke the strategic business decisions (PwC, 2012). And this situation is mainly caused by the fact that the GCC firms have not developed and implemented effective executive compensation schemes and plans in which more attractive incentives, schemes, plans relating to both behaviour-oriented and outcome-oriented compensation is provided to the executives working in the GCC firms.

We do not find a significant relationship between managerial ownership and total executive compensation. In this regard, findings of Cadbury report (1992) are highly relevant for the managerial ownership, particularly when there is no association between managerial ownership and executive compensation (Dahya et al., 2002). This indicates that there exists no relationship between managerial ownership and executive compensation. Moreover, Main and Johnson (1993) explain that making a relationship between managerial ownership and executive compensation not only increases corporate performance but it also diminishes the agency conflict as well. In other words, the alignment of shareholders and directors' interests will be reported and the agency relationship will be improved if a correlation is developed between managerial ownership and executive compensation. For example, some authors highlight that the total executive compensation is considerably less than in management-controlled firms (Bryan et al., 2000; Fich and Shivdasani, 2005).

In this regard, Abor and Biekpe (2007), highlight that this type of ownership empowers employees to feel the sense of attachment with firm and they continue to perform in a better way for obtaining better results for the overall firm performance. However, this finding is largely in contradiction with the results provided (for the period from 1998 to 2002) by Moustafa (2005) who found that owner-controlled firms comparatively performed better when they were compared with the performance of management-controlled firms. In the owner-controlled firm structure, major management, financial, and non-financial decisions are taken by the owner whereas in the management controlled firms, the strategic decision making structure is decentralised in which different department heads are empowered to take relevant and effective decisions. These studies clearly demonstrate that the previous research in the UK and the US and in the GCC countries has resemblance with the findings of this paper.

Ownership concentration has a negative relationship with total executive compensation at 1 per cent significance level in most of the models. In this regard, it is important to mention that majority of empirical studies do not paint a clear picture of executive compensation and ownership concentration. It is highlighted by the literature that in companies with a high ownership concentration (Schmidt 1997; Elston and Goldberg, 2003). Overall, for GCC countries, the firms with higher ownership concentration are not inclined to provide higher executive compensation to the directors.

In the board characteristics, the findings indicate that board size retains positive relationship with the determinants of total executive compensation. Previous literature has found a significant role of the board in the matter of executive compensation, and the board represents an important internal control mechanism to monitor the compensation schemes (Raheja, 2005). However, Dalton et al. (1999) did not find any evidence of a relationship between board size and firm performance and consequently on executive compensation. On the other hand, Guest (2009) found an increase in the CEO pay with an increase in the size of the board in respect of 1880 public firms in the UK. Core et al. (1999) found larger boards to provide increased levels of executive compensation in the context of United States. With a smaller board size, the board members will be more comfortable and compatible with the overall board performance in which their individual role and efforts will be appropriately rewarded and compensated as well (Dalton et al. 1999)

In addition, only chairman family in Model 2 retains positive correlation with the determinants of total executive compensation. In this regard, Al-Saidi and Al-Shammari (2013) have highlighted that in Kuwait, company law allows the role duality in which a single person can assume both roles (CEO and board Chairman) simultaneously. And due to this, the Kuwait banking industry have improved its financial performance and have incorporated and subscribed to numerous corporate governance benchmarks.

External ownership also retains positive relationship with the total executive compensation at 10 per cent statistical significance level in Model 6. In other words, the sample also reflects that increase in external ownership will also improve the level and type of executive compensation. Ownership structure has been found to be one of the

important aspects of corporate governance system with the effectiveness of monitoring increasing with concentrated ownership.

4.3.2.2 Determinants of Salaries

Salary remains an important part of executive compensation. In this regard, it is important to highlight that some companies do not report salary and other fringe benefits in their annual reports. Consequently, it becomes highly essential for this study to discuss salary separately and highlight main related issues with it. In addition, both salary and bonus are analysed separately as the former represents the behaviour-oriented compensation and the latter reflects the outcome-oriented compensation. Due to their separate effect on the motivational level of executives, both indicators have been separately used.

We present results in Table 4.5 and follow a similar format of running different models as above in section 4.3.2.1. The study finds a positive and statistically significant relationship between firm size and executive salary. In addition, the study reports a positive and significant impact of leverage on salaries paid to top five executives in most of the models.

In addition, the positive relationship between firm size in all six models and for leverage in 3, 4, 5 and in Model 6, can be attributed to the fact that executive compensation is more closely related to the size of the firm when the size is measured by the quantum of sales and in some cases by the profits made by the companies. This finding has more bearing on the application of agency theory to the facet of executive compensation. This relationship reveals the fact that with the increase in the sales, the CEOs may be paid more which in turn will induce them to work towards maximising the sales (Hijazi and Bhatti, 2007). It is because the CEOs are more likely to put their additional efforts to increase the size so that they can maximise their compensation (Tosi et al., 2000). The situation may be different in the context of GCC countries in the case of many companies where there might not be any positive and significant relationship between executive compensation and firm size/performance because of the large prevalence of family ownership. In the literature there is evidence for the absence of a positive relationship between firm performance and executive pay. For example, Gregg et al.

Table 4.5 Determinants of the salaries

This table presents coefficient estimates for pooled OLS regressions estimating the relationship between corporate governance variables and performance. Industry, year and country dummy variables control for the macroeconomic conditions. Robust standard errors are reported in parenthesis. ***, ** and * represents significance levels at 1%, 5% and 10%, respectively. See Table 4.1 for exact definitions of variables.

	Model 1	Model 2	Model 3	Model 4	Model 5	Model 6
Financial and economic characteristics						
Firm size	0.42***	0.39***	0.28***	0.25***	0.28***	0.29***
	(0.06)	(0.06)	(0.05)	(0.07)	(0.06)	(0.05)
Leverage	-0.01	0.16	0.82*	0.92**	0.99**	0.77*
	(0.55)	(0.53)	(0.43)	(0.43)	(0.44)	(0.41)
Market to book	0.30	0.01	-0.05	-0.05	-0.05	-0.05
	(0.02)	(0.02)	(0.06)	(0.06)	(0.06)	(0.05)
Return on assets (ROA)	0.49	0.39	0.65	0.68	0.62	0.63
	(0.72)	(0.69)	(0.91)	(0.90)	(0.91)	(0.91)
Board Characteristics						
Board size		0.34	0.61*	0.54	0.63*	0.60
		(0.27)	(0.36)	(0.38)	(0.36)	(0.37)
Chairman family		-0.38***	-0.48***	-0.45***	-0.49***	-0.46***
		(0.14)	(0.16)	(0.17)	(0.16)	(0.17)
Independent directors		0.13	0.31	0.32	0.31	0.36
		(0.17)	(0.24)	(0.24)	(0.23)	(0.23)
Executive directors		-1.67***	-2.12***	-2.16***	-2.09**	-1.77**
		(0.68)	(0.82)	(0.82)	(0.86)	(0.77)
Ownership Structure						
Concentrated ownership			-0.15**	-0.16	-0.05	-0.11
			(0.07)	(0.07)	(0.05)	(0.09)
Managerial ownership			0.02***	0.02***	0.01**	
			(0.01)	(0.01)	(0.01)	
Institutional investor ownership			0.01**	0.01**		
			(0.49)	(0.49)		
Family ownership			0.01	8.99	-0.89	
			(0.48)	(0.48)	(0.49)	
Foreign ownership				0.21		
				(0.22)		
Government ownership					0.43	
					(0.62)	
External ownership						0.01
						(0.01)
Industry dummy variables	Yes	Yes	Yes	Yes	Yes	Yes
Year dummy variables	Yes	Yes	Yes	Yes	Yes	Yes
Country dummy variables	Yes	Yes	Yes	Yes	Yes	Yes
Number of observations	538	538	373	373	373	373

(2005) found little relationship between these two variables. This situation is found in the findings in Model 3 where the absence of relationship between managerial ownership, institutional ownership and foreign ownership with the determinants of total executive compensation, reflecting that only family ownership is relevant and related to the firms operating in the GCC countries.

In this regard, it is important to highlight that this mainly reflects the GCC firms where business environment is considerably different from the UK and US business environment when it is compared with the business climate existing in other parts of the world. Moreover, Mohan and Ainina (2012) argue that higher executive compensation, which also includes salary, is not a choice but a corporate requirement and compulsion as well. This is mainly caused by the fact that executives hiring trend has increased executive compensation throughout the corporate world. If this statement is applied to the findings of this study, it can be argued that the GCC firms follow this rule as they are required to provide market-based incentives to their current and potential top executives.

We do not find any relationship between ROA and salary. In this situation, the GCC firms are more inclined to pay salary rather than bonus. In other words, it is difficult for the GCC firms to highlight the marginal productivity of their executives[21]. This is in contradiction with the real business world practices in which the executive compensation is connected to the ROA. In addition, in the context of agency theory, this alignment is largely visible because directors and shareholders are needed to have similar corporate objectives and priorities through which they can work together and avoid any chances of agency conflict. Principal-agent theory considerably relies on the use of arm's length contracting between shareholders and managers (Bruce et al., 2005). Within the same context, Buck et al. (2003) explain that market-based executive compensation is highly essential for obtaining and retaining a lucrative financial corporate performance.

In terms of board characteristics the results indicate to a positive relationship between salary and board size, although this is only supported in Models 3 and 5. On the other hand, the research finds a significant negative relationship between chairman family and

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[21] Marginal productivity is additional contribution provided by executive to the productivity of firm. In other words, cost of absence of those executives will be computed in case that executive withdraws executive services from the board.

salary in all models. In other words, behaviour-oriented compensation in the shape of salary has no attraction for chairman family as the family run companies are owned and run by the families who are more interested to use their will rather than corporate governance practices for evaluating and rewarding family executives.

We report a negative and statistically significant relationship between the executive board and salary. This finding is in line with previous studies. For example Union of Arab Banks (2007) found that in the GCC countries boards do not have a majority presence of independent members. Hence, the major strategic decisions of boards are compromised[22].

Regarding ownership, the study does not find significant coefficients for family, foreign, government and external ownership. Results are similar to Al-Tamimi (2012) in terms of government ownership. It is found that ownership concentration has significant negative relationship with salaries, but only in Model 3. In other words, the higher the ownership concentration, the lower the salaries would be in GCC countries. In this regard, it is important to mention that the similar finding has also been highlighted by Andreas et al. (2010) for Germany.

The coefficient of managerial ownership variable is positive and statistically significant in Models 3-5. This is an important finding. Andreas et al. (2010) found the presence of negative relationship between management ownership and result-oriented compensation. The result-oriented compensation is more important and comprehensive variable when it is compared with the salary, Based on both these results, it can be highlighted that the GCC firms increase executive compensation when managerial ownership is increased.

Institutional ownership also maintains positive and significant relationship with salary. This shows that the higher the institutional ownership the higher the executive salaries. In this regard, Hartzell and Starks (2003) found that the higher institutional ownership offers lower managerial compensation and salary because they closely monitor the performance of directors. Consequently, this close supervision enables the institutional investors to appropriately evaluate the managerial performance of directors and determine their actual level of executive compensation. This can be explained by the institutional

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[22] The higher salaries will not increase board effectiveness.

investors, who mainly represent foreign investors, are more capable of assessing firms, executive's contribution to firm's previous and current operational and financial standing.

4.3.2.3 Determinants of the Bonuses

Table 4.6 presents results for the regressions where bonus is used as dependent variable. In addition, it is important to mention that in the collected and regressed GCC data, not all firms publically announce and report all types of executive bonuses for the directors. Consequently, it becomes highly essential to use different strategy for analysing the results. One significant finding is the positive and significant relationship between market to book value bonuses paid to executives.

The relationship between firm size and bonus is positive. In this regard, Eisenhardt (1989) maintains that within the context of outcome-oriented compensation (e.g. bonus), the agency theory highlights that the outcome-oriented compensation is more capable to align managerial interests with the interest of shareholders. Based on this narrative, it can be deduced that the larger firms have put in place a strong and attractive outcome-based compensation plans which motivates them to provide their best efforts for attaining maximum corporate results. Through this mechanism, alignment of interests between both directors and shareholders is largely experienced and observed. Recently, in 2010, in Saudi Arabia SAMA has developed a framework pertaining to executive compensation for top banking executives in which it has also proposed the establishment of Nomination and Remuneration Committees as well (Everett and Drabich, 2010). Before this corporate governance mechanism, the directors did not find any mechanism aligning their interests with shareholders' interests. Consequently, higher chances of agency cost were unavoidable particularly in Saudi Arabia and other GCC countries where such mechanisms were not present. However, after 2008 global financial crisis, many GCC countries, especially Saudi Arabia, introduced above corporate governance mechanisms which provide an opportunity to experience alignment of interests between directors and shareholders. These studies highlight the

Table 4.6 Determinants of the bonuses

This table presents coefficient estimates for pooled OLS regressions estimating the relationship between corporate governance variables and performance. Industry, year and country dummy variables control for the macroeconomic conditions. Robust standard errors are reported in parenthesis. ***, ** and * represents significance levels at 1%, 5% and 10%, respectively. Definitions for all the variables are provided in Table 4.1.

	Model 1	Model 2	Model 3	Model 4	Model 5	Model 6
Financial and economic characteristics						
Firm size	0.23***	0.16*	0.21**	0.11	0.16	0.17
	(0.07)	(0.08)	(0.11)	(0.13)	(0.12)	(0.11)
Leverage	-0.48	-0.55	-1.01	-0.72	-0.85	-0.82
	(0.52)	(0.53)	(0.71)	(0.78)	(0.78)	(0.72)
Market to book	0.07***	0.07***	0.11*	0.12*	0.11*	0.11*
	(0.03)	(0.02)	(0.06)	(0.06)	(0.06)	(0.06)
Return on assets (ROA)	0.39	0.46	0.13	0.22	0.15	0.05
	(0.91)	(0.95)	(0.01)	(0.01)	(0.12)	(0.01)
Board Characteristics						
Board size		1.34**	1.12	0.92	1.16	0.94
		(0.21)	(0.70)	(0.71)	(0.70)	(0.69)
Chairman family		0.39*	0.31	0.39	0.33	0.59**
		(0.21)	(0.27)	(0.27)	(0.27)	(0.26)
Independent directors		-0.08	0.23	0.25	0.27	0.17
		(0.47)	(0.64)	(0.65)	(0.65)	(0.63)
Executive directors		1.53	1.93	1.82	2.13	2.85*
		(1.23)	(1.70)	(1.71)	(1.75)	(1.59)
Ownership Structure						
Concentrated ownership			-0.03	-0.05	-0.09	-0.02
			(0.15)	(0.15)	(0.11)	(0.14)
Managerial ownership			0.01*	0.02**	0.02***	
			(0.90)	(0.95)	(0.01)	
Institutional investor ownership			-0.28	-0.24		
			(0.96)	(0.87)		
Family ownership			0.01*	0.01*	0.01*	
			(0.63)	(0.64)	(0.01)	
Foreign ownership				0.61		
				(0.45)		
Government ownership					0.01	
					(0.01)	
External ownership						0.02
						(0.76)
Industry dummy variables	Yes	Yes	Yes	Yes	Yes	Yes
Year dummy variables	Yes	Yes	Yes	Yes	Yes	Yes
Country dummy variables	Yes	Yes	Yes	Yes	Yes	Yes
Number of observations	538	538	373	373	373	373

current endeavour of GCC firms for incorporating both types of executive compensation in their governance structure.

Gavin (2010) points out that the family-owned firms face the financial problems in Saudi Arabia. In addition, Baydoun et al. (2013) maintain that ineffective scrutiny and inadequate transparency and disclosure measures are some of the common corporate governance problems found in the Saudi Arabia. However, the findings of this study highlight that the family-owned firms have positive correlation with bonus, highlighting that directors are only interested to resolve the operational issues such as effective assessment of executives' marginal productivity.

The relationship between bonus and chairman family is also pertinent and positive within the context of the GCC countries. In this regard, Mishra et al. (2001) highlight that family ownership reduces agency cost. In other forms of ownership, agency relationship and agency costs are higher and create different organisational and managerial issues and problems as well. However, in the family ownership in which the chairman runs the board affairs like family affairs, the chances of diminishing agency conflict are higher as family members use family traits, paternalism and altruism for avoiding conflict and agency problems as well (James, 1999). In this regard, it is important to highlight that outcome-oriented compensation is subjective and it is based on the wish of board chairman. Consequently, it is easier to reward this compensation to family members. Overall, the relationship between bonus and executive directors also highlights no relationship except for Model 6 which is at 10 per cent statistical significance. On the contrary, the study findings reveal that the independent board exhibits no or limited relationship with bonus.

4.3.2.4 The choice between performance and behaviour oriented compensation

So far, the study has looked at determinants of total executive compensation and its components, salary, and bonus, separately. Here, the study presents results for our analysis of the determinants of the choice between bonus, performance-oriented compensation, and salary, and behaviour-oriented compensation. Using identical set of

exogenous variables, the study utilised bonus to total compensation as the dependent variable in the regressions. Results are presented in Table 4.7. It is found that firm's size

Table 4.7 Determinants of the choice between bonus and salary

This table presents coefficient estimates for pooled OLS regressions estimating the relationship between corporate governance variables and performance. Industry, year and country dummy variables control for the macroeconomic conditions. Robust standard errors are reported in parenthesis. ***, ** and * represents significance levels at 1%, 5% and 10%, respectively. Definitions for all the variables are provided in Table 4.1.

	Model 1	Model 2	Model 3	Model 4	Model 5	Model 6
Financial and economic characteristics						
Firm size	0.01*	0.01	0.02***	0.02*	0.02*	0.02**
	(0.69)	(0.75)	(0.85)	(0.97)	(0.01)	(0.01)
Leverage	0.04	0.03	-0.06	-0.04	-0.05	-0.07
	(0.05)	(0.05)	(0.06)	(0.06)	(0.06)	(0.06)
Market to book	0.49*	0.49**	0.01	0.01	0.01	0.01
	(0.25)	(0.24)	(0.72)	(0.01)	(0.01)	(0.01)
Return on assets (ROA)	0.04	0.03	0.01	0.01	0.01	0.01
	(0.08)	(0.08)	(0.10)	(0.10)	(0.10)	(0.10)
Board Characteristics						
Board size		0.05	0.58	-0.36	0.01	0.10
		(0.04)	(0.05)	(0.05)	(0.05)	(0.05)
Chairman family		0.04**	0.01	0.01	0.01	0.02
		(0.02)	(0.02)	(0.02)	(0.02)	(0.02)
Independent directors		-0.09	-0.09	-0.08	-0.08	-0.08
		(0.04)	(0.06)	(0.06)	(0.06)	(0.06)
Executive directors		0.12	0.19*	0.19*	0.22*	0.27**
		(0.09)	(0.11)	(0.11)	(0.11)	(0.11)
Ownership Structure						
Concentrated ownership			-0.07	-0.18	-0.01*	-0.02
			(0.01)	(0.01)	(0.88)	(0.01)
Managerial ownership			0.11	0.14	0.18**	
			(0.09)	(0.09)	(0.08)	
Institutional investor ownership			-0.09	-0.08		
			(0.07)	(0.07)		
Family ownership			0.01	0.02	0.02	
			(0.07)	(0.07)	(0.07)	
Foreign ownership				0.03		
				(0.03)		
Government ownership					0.06	
					(0.07)	
External ownership						0.07
						(0.07)
Industry dummy variables	Yes	Yes	Yes	Yes	Yes	Yes
Year dummy variables	Yes	Yes	Yes	Yes	Yes	Yes
Country dummy variables	Yes	Yes	Yes	Yes	Yes	Yes
Number of observations	538	538	373	373	373	373

is positive and statistically significant in almost all models. This shows that larger firms prefer to pay bonus as the main form of executive compensation. It is found that in the baseline models (1 and 2) coefficient of market to book value is statistically significant and positive. However, after the introduction of other variables to the model, this variable loses its significance.

In terms of board characteristics our only strongly significant variable that is related to the dependent variable is executive directors. However, critics of executive compensation are of the opinion that the board does not have any say in designing the executive compensation when the CEO has more power on the board (Core et al., 1999). Fama and Jensen (1983) point out the outside directors who are not affected by the CEO power are more likely to monitor the management actions effectively so that they can protect their reputation. On the other hand, when the outside directors have only insufficient information about the firm dealings of if they are appointed by the CEO then they are likely to perform only less effectively. Therefore, the finding that board characteristic has a strong influence on the executive compensation has to be considered in the light of these previous findings.

We also find some evidence that managerial ownership influences payment of more bonuses. Abor and Biekpe (2007) highlight that managerial ownership promotes the sense of ownership through soft scrutiny measures which encourage employees work harder. However, a growing body of literature that examines the relationship between managerial ownership, firm performance and executive compensation has explored the compensation aspect from different perspectives yielding mixed results. For example, Core et al. (1999) found high ownership concentration of CEOs to be a decreasing function in deciding the executive compensation. Similar research conducted in New Zealand by Gunasekaragea and Wilkinson (2002) and in Japan by Basu et al. (2007) documented a positive relation between managerial compensation and firm performance. Zhu et al. (2009) examined the influence of managerial ownership on executive compensation in China and found a strong relationship between managerial pay and performance in the case of privately-controlled firms.

Ownership concentration retains negative relationship with the determinants of the choice between salaries and bonuses, but only in Model 5. This indicates that if the company has

a few controlling owners, they prefer to use the measure of salary for motivating directors. To understand this, ownership concentration needs to be elaborated further. For example, Gul et al. (2010) state two types of effects are provided by ownership concentration: managerial entrenchment effect and incentive alignment effect. Under the framework of managerial ownership concentration structure, owners are more powerful and at their will to use resources and policies at the cost of other stakeholders including employees and shareholders (Fan and Wong, 2002). Consequently, the results of this study also highlight that a few owners will not be accountable for their executive decisions and they will have greater leverage to control executives rather than professionally satisfying them.

4.3.2.5 Robustness Check

4.3.2.5.1 Lagged variables

To check the robustness of our results, we repeat our pooled OLS regressions with lagged values for independent firm characteristics variables. First, in Table 4.8 (Appendix A) we re-estimate the regressions models with lagged values for firm characteristics variables for checking the results in respect of determinants of total executive compensation. We find that the results of the robustness check have not shown any significant deviations from the findings of the pooled OLS regression done earlier in the case of the variables of firm size, leverage, market to book and return on assets where one year lag variables are used for testing. However, the coefficients in respect of other variables like managerial ownership, institutional investor ownership, family ownership, foreign ownership, government ownership and external ownership show significant deviations from the original findings. Thus, the ownership structure seems to show significantly different effect on firm performance when one year lag values are used for testing the robustness of the results. For example, in the case of managerial ownership a higher level of positive relationship with firm performance has been reported in the robustness test. The deviation is observed in the case of all models tested.

Second, we re-estimate the regressions models with lagged values for firm characteristics variables for checking the results in respect of determinants of salaries. Results of the robustness check are reported in Table 4.9 (Appendix A). We find that the findings from the robustness check in the case of variables like leverage and return on assets show

insignificantly higher positive relationship between these financial and economic characteristics and firm performance. For example, in the case of variable leverage while the original OLS regression showed a statistically insignificant negative relationship, the robustness check results show a statistically insignificant positive relationship. We observe a comparatively lesser deviation in the case of the variable firm size. Slight variations have been observed in the case of board characteristic variables as well as in the ownership structure variables in the robustness check.

Third, in Table 4.10 (Appendix A) we re-estimate the regressions models with lagged values for firm characteristics variables for checking the results in respect of determinants of bonuses. We find that the results of the robustness checks strongly support the findings from the original OLS regression. The coefficients from the robustness check in respect of financial and economic characteristics have shown the same trend. In the case of variables like return on assets while the original OLS regression showed a statistically insignificant positive relationship, the robustness check results show a statistically insignificant negative relationship. We observe a comparatively lesser deviation in the case of the variable firm size and market to book. Slight variations have been observed in the case of board characteristic variables as well as in the ownership structure variables in the robustness check.

Finally, we re-estimate the regressions models with lagged values for firm characteristics variables for checking the results in respect of determinants of the choice between bonus and salary. Results of the robustness check using lag values are reported in Table 4.11 (Appendix A). From the findings we observe that there are no statistically significant variations in the coefficients in the case of financial and economic characteristic variables of firm size and leverage out of our regression to check the robustness of the original findings. In the case of these variables we used one year lag values to run the robustness tests. However, in the case of market to book we observe significant variation from the original findings with confidence levels of both 5% and 10% indicating a positive relationship between determinants of the choice between bonus and salary and firm performance. This type of variation is observed in all the six models tested for robustness. We also observe statistically insignificant variations in the case of variables covered under board characteristics and ownership structure.

4.3.2.5.2 Interactions Variables

We repeat our results of the estimations for the regressions models of interacting variables with various ownership variables. We interact concentrated with managerial ownership, concentrated with family ownership, concentrated with external ownership and lastly managerial with family ownership to test whether the new interacted variables make a difference. The tests are intended to check the robustness of the original findings and the variations in the relationship because of the inclusion of new interaction variables in the regression. The regression results are presented in Table 4.12 (Appendix A). We observe no variations in the coefficients for firm size, leverage, market to book and return on assets while considering the robustness check for the determinants of total executive compensation. We also observe statistically insignificant variations in the case of board size, independent directors, executive directors and concentrated ownership.

In Table 4.13 (Appendix A) the results of the robustness check conducted using interaction variables are presented. While we observe no variations in the coefficients for firm size and return on assets we find observable variations in respect of leverage and market to book indicating more negativity in the case of leverage and more positivity in the case of market to book while considering the robustness check for the determinants of the choice between bonus and salary. We also observe statistically insignificant variations in the case of board size, independent directors, executive directors and concentrated ownership. These variations have been observed over all the models.

4.3.2.5.3 Two-Stages Least Squares (2SLS) Regression

In many of the econometric analyses, the framework of y on x regression does not represent a perfect theoretical relationship. This is because of the impact of the omitted variables on the relationship or the presence of errors-in-variables or measurement error in the x variables. In these cases, the pooled Ordinary Least Squares (OLS) may not have the capability to deliver consistent parameter estimates. Under such circumstances, instrumental variable estimator is employed in the context of endogeneity and regression tests conducted, which is known as Two-Stages Least Squares. Using a system of simultaneous equations and adopting a two-stages least squares (2SLS) regression may,

to some extent, alleviate the endogeneity effects on the results. In order to remove the endogeneity effects, we employed 2SLS regression models with suitable endogeneity and instrumental variables.

In order to remove the endogeneity and check the robustness of the findings from the earlier regression models in respect of the determinants of total compensation, we undertook 2SLS regression with Return on Assets (ROA) as endogeneity variable and GDP growth and Free Cash Flow as instrumental variables. In the corporate governance literature, firm level performance is identified with three main approaches − market prices, accounting ratios, and total factor profitability (Brown and Caylor, 2004). Using accounting ratios like ROA is common in research studies because ROA shows the profitability of the company in relation to its total assets and it has a strong relationship with leverage and firm size (Bocean & Barbu, 2007). The better the leverage of the company, the stronger is the ROA. Factors like leverage and firm size can also be considered as determining the total executive compensation. Moreover, the ROA-corporate governance link reflects a tangible balance sheet effect devoid of endogeneity (Vintila and Gherghina, 2012). Therefore, this study proposed to use ROA as endogeneity variable. GDP growth was selected as instrumental variables because, in general, the well-being of an economy will augment the profitability of a company operating within the economy and thus contribute to better ROA. At the same time, GDP growth does not automatically have a relationship with total executive compensation. Free cash flow was chosen as an instrumental variable because it has a direct relationship with ROA. With higher returns, the cash flow of the company increases which in turn becomes instrumental for better accounting ratio of ROA.

The results of the 2SLS regression tests with respect to determinants of total executive compensation are presented in Table 4.14 (Appendix A). The comparison of the findings of 2SLS regression as reported in Table 4.14, with the results of the earlier pooled OLS regression tests, shows, that while the coefficient values for firm characteristics like firm size, leverage, and market to book do not show any statistically significant variations, the positivity in the relationship between ROA and firm performance has gone down significantly. This proves that ROA as an endogeneity variable has much influence on the determination of total executive compensation. In the case of board characteristics, while the variable board size has been significantly affected, we find small variations in the

coefficient values of other variables that are not significant. While comparing the effect on ownership variables, the 2SLS regression has produced significant variations in concentrated, managerial, institutional investor, family, foreign, government, and external ownership variables. This result implies a strong impact of ownership structure on total executive compensation.

Second, we re-estimate the regressions models for two-stages least squares (2SLS) with determinants of the choice between bonus and salary. The results of the 2SLS regression tests are presented in Table 4.15 (Appendix A). The results indicate a significant variation in the case of market-to-book and an insignificant variation in respect of ROA. We do not observe any statistically significant variation in respect of other firm characteristic variables. In the case of board characteristics, although we notice some variations in the coefficient values resulting from 2SLS regression, they are not statistically significant, implying that the revised regression estimates support the findings from the original regression tests. In respect of ownership structure variables, we find that there are significant variations in the coefficient values, indicating a strong influence of ownership criteria on the determinants of the choice between bonus and salary.

4.4   Conclusion

Executive compensation mainly encompasses behaviour-oriented and outcome oriented compensation. Here we explore the determinants of the executive compensation in the GCC countries using a sample of 349 listed firms located in five GCC countries (Kuwait, Oman, Qatar, Saudi Arabia and United Arab Emirates) within a time period between 2006 and 2011 by looking at the compensation paid to the top five executives. In particular the study aimed at how total compensation and its components as behaviour (salary) and outcome (bonus) oriented are shaped by firm characteristics, ownership structure and other corporate governance mechanisms. Additionally, the study examined the determinants of the choice of compensation type (namely behaviour versus outcome) by the GCC firms.

We find that in the GCC countries larger firms and firms with potential future growth pay higher total compensation to their executives. Concentrated ownership structure leads to

lower compensation levels while firms with high family ownership then to pay higher compensation. There is also evidence that external ownership leads to higher total compensation. In terms of behaviour-oriented compensation (i.e. salary), the study finds that larger firms and firms with higher leverage pay higher salaries to executives. Firms that have a chairman from the family and have higher presence of executive members in the board tend to pay lower salaries. The study also found that managerial as well as institutional ownership of companies tends to lead to higher salaries. In terms of outcome-oriented compensation (i.e. bonus), the study found evidence that companies that has more growth potential pay higher bonuses. A family related chairman and higher number of executive members in the board is related positively to bonus payments. There is also evidence that ownership by managers and by family results in higher levels of outcome-oriented compensation. The study finds that the choice between behaviour versus outcome oriented compensation is mainly influenced by firm size, the presence of executive members on the board and managerial ownership. Companies that have higher number of executives or owned by managers pay more compensation through bonuses.

From the 2SLS regression results, it is learnt that the value of executive compensation while having a direct relationship with the firm size, the variable has also been subjected to the influence of instrumental variables like board members and managerial ownership. This study also undertook robustness check using one year lagged values for firm characteristic variables. The robustness check has not revealed any significant variations from the findings of the original pooled OLS regression results in the case of the variables of firm size, leverage, market to book and return on assets while checking for determinants of total executive compensation, where one year lag variables are used for testing. The findings from the robustness check in the case of variables like leverage, market to book and return on assets show a significantly higher positive relationship between these financial and economic characteristics and firm performance when checked for the determinants of salaries. While checking for the determinants of the choice between bonus and salary the original pooled OLS regression showed a statistically insignificant negative relationship; but the robustness check results show a statistically significant positive relationship.

This research might have suffered from some limitations affecting the findings to a certain extent. One of the major methodological limitations of this research pertains to the data

collected for analysis. The limitation arose because of the reporting practices of companies operating within the GCC region. For example, it is not the practice of all companies in the GCC countries to report complete data pertaining to the top five executives. While some companies present a composite figure of total executive compensation without any break-down of details, other companies follow the practice of reporting the salaries and bonus separately. There are also companies that report only salaries without any mention of other payments made to the executives. Lack of extensive research on the executive compensation in Gulf countries presented a limitation in building up a sound theoretical background to the research.

Further research is needed with focus on additional measures that are not dealt with by this research. Such further research may involve finding additional constructs and study their impact on the levels and structures on executive compensation in the Gulf region. For instance, further research may examine role duality and CEO control over boards of GCC firms and presence of independent directors to assess the extent of their impact in the determination of executive compensation. Corporate governance is another area that offers scope for further extensive research for its impact in deciding compensation structures in the GCC firms. Since the changes in the economic and political environments are likely to bring about many changes in corporate governance mechanisms of GCC countries, a comparative study of the latest changes in corporate governance measures in GCC countries with those being followed in developed countries in so far as they affect the executive compensation levels is likely to provide extended knowledge on the determination of executive compensation by companies in the GCC region. For example, the effect of formation of remuneration committees in the board and its impact on the determination of compensation in GCC countries as compared to Western countries is a probable area of further research.

Appendix A

Table 4.8 Determinants of total executive compensation-Lagged Financial and economic characteristics

This table presents coefficient estimates for pooled OLS regressions estimating the relationship between corporate governance variables and performance. Industry, year and country dummy variables control for the macroeconomic conditions. Robust standard errors are reported in parenthesis. ***, ** and * represents significance levels at 1%, 5% and 10%, respectively. Definitions for all the variables are provided in Table 4.1.

	Model 1	Model 2	Model 3	Model 4	Model 5	Model 6
Financial and economic characteristics						
Firm size (1 year lag)	0.492***	0.484***	0.461***	0.457***	0.471***	0.464***
	(0.021)	(0.023)	(0.030)	(0.031)	(0.031)	(0.029)
Leverage (1 year lag)	0.130	0.126	0.282	0.293	0.237	0.275
	(0.135)	(0.137)	(0.184)	(0.189)	(0.191)	(0.181)
Market to book (1 year lag)	0.004***	0.004***	0.004***	0.004***	0.004***	0.004***
	(0.001)	(0.001)	(0.001)	(0.001)	(0.001)	(0.001)
Return on assets (1 year lag)	0.002	0.002	-0.001	-0.001	-0.001	-0.001
	(0.002)	(0.002)	(0.003)	(0.003)	(0.003)	(0.003)
Board Characteristics						
Board size		0.183	0.294	0.288	0.266	0.239
		(0.137)	(0.173)	(0.171)	(0.170)	(0.168)
Chairman family		0.108	0.018	0.023	0.013	0.054
		(0.057)	(0.074)	(0.074)	(0.074)	(0.068)
Independent directors		0.142	0.228	0.229	0.207	0.231
		(0.150)	(0.197)	(0.198)	(0.195)	(0.191)
Executive directors		-0.151	0.043	0.046	-0.004	0.195
		(0.258)	(0.358)	(0.359)	(0.357)	(0.350)
Ownership Structure						
Concentrated ownership			-0.107**	-0.109**	-0.062*	-0.136***
			(0.036)	(0.036)	(0.027)	(0.035)
Managerial ownership			0.005	0.006	0.003	
			(0.004)	(0.004)	(0.003)	
Institutional investor ownership			0.003	0.003		
			(0.002)	(0.002)		
Family ownership			0.005	0.005	0.004	
			(0.003)	(0.003)	(0.002)	
Foreign ownership				0.041		
				(0.078)		
Government ownership					-0.003	
					(0.003)	
External ownership						0.006**
						(0.002)
Industry dummy variables	Yes	Yes	Yes	Yes	Yes	Yes
Year dummy variables	Yes	Yes	Yes	Yes	Yes	Yes
Country dummy variables	Yes	Yes	Yes	Yes	Yes	Yes
Number of observations	1,254	1,249	866	866	866	866

Table 4.9 Determinants of the salaries-Lagged Financial and economic characteristics

This table presents coefficient estimates for pooled OLS regressions estimating the relationship between corporate governance variables and performance. Industry, year and country dummy variables control for the macroeconomic conditions. Robust standard errors are reported in parenthesis. ***, ** and * represents significance levels at 1%, 5% and 10%, respectively. See Table 4.1 for exact definitions of variables.

	Model 1	Model 2	Model 3	Model 4	Model 5	Model 6
Financial and economic characteristics						
Firm size (1 year lag)	0.381***	0.360***	0.295***	0.279***	0.315***	0.315***
	(0.032)	(0.035)	(0.049)	(0.058)	(0.055)	(0.046)
Leverage (1 year lag)	0.357	0.493	0.673	0.713	0.771	0.593
	(0.319)	(0.349)	(0.454)	(0.439)	(0.460)	(0.422)
Market to book (1 year lag)	-0.010	-0.006	-0.039	-0.039	-0.027	-0.030
	(0.020)	(0.019)	(0.042)	(0.042)	(0.040)	(0.040)
Return on assets (1 year lag)	0.011	0.009	0.009	0.009	0.010	0.010
	(0.008)	(0.007)	(0.010)	(0.009)	(0.010)	(0.010)
Board Characteristics						
Board size		0.304	0.378	0.336	0.404	0.402
		(0.255)	(0.335)	(0.362)	(0.344)	(0.350)
Chairman family		-0.315*	-0.346*	-0.333*	-0.353*	-0.378*
		(0.144)	(0.141)	(0.154)	(0.143)	(0.169)
Independent directors		0.165	0.194	0.194	0.174	0.262
		(0.159)	(0.207)	(0.207)	(0.206)	(0.197)
Executive directors		-1.368*	-1.789*	-1.821*	-1.845*	-1.581
		(0.680)	(0.849)	(0.826)	(0.892)	(0.820)
Ownership Structure						
Concentrated ownership				-0.198**	-0.202**	-0.065	-0.153
			(0.066)	(0.069)	(0.049)	(0.082)
Managerial ownership				0.017*	0.018*	0.010	
			(0.008)	(0.008)	(0.007)	
Institutional investor ownership				0.011*	0.011*		
			(0.005)	(0.005)		
Family ownership				-0.002	-0.002	-0.003	
			(0.005)	(0.005)	(0.006)	
Foreign ownership					0.098		
				(0.211)		
Government ownership						0.001	
					(0.005)	
External ownership							0.009
						(0.005)
Industry dummy variables	Yes	Yes	Yes	Yes	Yes	Yes
Year dummy variables	Yes	Yes	Yes	Yes	Yes	Yes
Country dummy variables	Yes	Yes	Yes	Yes	Yes	Yes
Number of observations	466	466	342	342	342	342

Table 4.10 Determinants of the bonuses-Lagged Financial and economic characteristics

This table presents coefficient estimates for pooled OLS regressions estimating the relationship between corporate governance variables and performance. Industry, year and country dummy variables control for the macroeconomic conditions. Robust standard errors are reported in parenthesis. ***, ** and * represents significance levels at 1%, 5% and 10%, respectively. Definitions for all the variables are provided in Table 4.1.

	Model 1	Model 2	Model 3	Model 4	Model 5	Model 6
Financial and economic characteristics						
Firm size (1 year lag)	0.279***	0.200*	0.156	0.074	0.093	0.119
	(0.072)	(0.089)	(0.104)	(0.137)	(0.119)	(0.108)
Leverage (1 year lag)	-0.277	-0.364	-0.669	-0.459	-0.516	-0.387
	(0.643)	(0.667)	(0.757)	(0.843)	(0.865)	(0.765)
Market to book (1 year lag)	0.114***	0.109***	0.165**	0.169**	0.158**	0.155**
	(0.031)	(0.028)	(0.053)	(0.053)	(0.051)	(0.051)
Return on assets (1 year lag)	-0.008	-0.007	-0.004	-0.003	-0.004	-0.004
	(0.012)	(0.012)	(0.016)	(0.015)	(0.016)	(0.015)
Board Characteristics						
Board size		1.184*	1.484	1.261	1.508	1.154
		(0.564)	(0.816)	(0.828)	(0.813)	(0.749)
Chairman family		0.235	0.250	0.318	0.260	0.570*
		(0.233)	(0.282)	(0.282)	(0.280)	(0.278)
Independent directors		-0.422	-0.132	-0.132	-0.092	-0.258
		(0.487)	(0.686)	(0.685)	(0.688)	(0.667)
Executive directors		1.835	2.376	2.207	2.637	3.206*
		(1.270)	(1.753)	(1.799)	(1.786)	(1.556)
Ownership Structure						
Concentrated ownership			0.119	0.099	-0.010	0.133
			(0.168)	(0.171)	(0.122)	(0.159)
Managerial ownership			0.013	0.017	0.019*	
			(0.011)	(0.012)	(0.010)	
Institutional investor ownership			-0.007	-0.007		
			(0.010)	(0.010)		
Family ownership			0.013	0.013	0.014	
			(0.007)	(0.007)	(0.008)	
Foreign ownership				0.519		
				(0.503)		
Government ownership					0.009	
					(0.009)	
External ownership						-0.006
						(0.009)
Industry dummy variables	Yes	Yes	Yes	Yes	Yes	Yes
Year dummy variables	Yes	Yes	Yes	Yes	Yes	Yes
Country dummy variables	Yes	Yes	Yes	Yes	Yes	Yes
Number of observations	466	466	342	342	342	342

Table 4.11 Determinants of the choice between bonus and salary-Lagged Financial and economic characteristics

This table presents coefficient estimates for pooled OLS regressions estimating the relationship between corporate governance variables and performance. Industry, year and country dummy variables control for the macroeconomic conditions. Robust standard errors are reported in parenthesis. ***, ** and * represents significance levels at 1%, 5% and 10%, respectively. Definitions for all the variables are provided in Table 4.1.

	Model 1	Model 2	Model 3	Model 4	Model 5	Model 6
Financial and economic characteristics						
Firm size (1 year lag)	0.017**	0.010	0.015	0.005	0.005	0.012
	(0.006)	(0.007)	(0.008)	(0.009)	(0.009)	(0.008)
Leverage (1 year lag)	0.049	0.039	0.005	0.030	0.030	0.002
	(0.049)	(0.049)	(0.058)	(0.061)	(0.062)	(0.058)
Market to book (1 year lag)	0.007**	0.006**	0.011*	0.011**	0.009*	0.009*
	(0.002)	(0.002)	(0.004)	(0.004)	(0.004)	(0.004)
Return on assets (1 year lag)	-0.001	-0.001	-0.000	-0.000	-0.000	-0.000
	(0.001)	(0.001)	(0.001)	(0.001)	(0.001)	(0.001)
Board Characteristics						
Board size		0.054	0.035	0.008	0.039	0.024
		(0.041)	(0.053)	(0.055)	(0.054)	(0.052)
Chairman family		0.020	0.011	0.020	0.013	0.022
		(0.021)	(0.025)	(0.025)	(0.024)	(0.024)
Independent directors		-0.139**	-0.123	-0.123	-0.117	-0.121
		(0.046)	(0.063)	(0.063)	(0.064)	(0.062)
Executive directors		0.140	0.230*	0.210	0.271*	0.282*
		(0.092)	(0.117)	(0.116)	(0.115)	(0.109)
Ownership Structure						
Concentrated ownership			0.010	0.008	-0.009	-0.003
			(0.013)	(0.014)	(0.009)	(0.012)
Managerial ownership			0.001	0.001	0.002	
			(0.001)	(0.001)	(0.001)	
Institutional investor ownership			-0.001	-0.001		
			(0.001)	(0.001)		
Family ownership			0.000	0.000	0.000	
			(0.001)	(0.001)	(0.001)	
Foreign ownership				0.061*		
				(0.029)		
Government ownership					0.001*	
					(0.001)	
External ownership						0.000
						(0.001)
Industry dummy variables	Yes	Yes	Yes	Yes	Yes	Yes
Year dummy variables	Yes	Yes	Yes	Yes	Yes	Yes
Country dummy variables	Yes	Yes	Yes	Yes	Yes	Yes
Number of observations	466	466	342	342	342	342

Table 4.12 Determinants of total executive compensation-Interaction variables

This table presents coefficient estimates for pooled OLS regressions estimating the relationship between corporate governance variables and performance. Industry, year and country dummy variables control for the macroeconomic conditions. Robust standard errors are reported in parenthesis. ***, ** and * represents significance levels at 1%, 5% and 10%, respectively. Definitions for all the variables are provided in Table 4.1.

	Model 1	Model 2	Model 3	Model 4	Model 5	Model 6	Model 7	Model 8	Model 9	Model 10
Financial and economic characteristics										
Firm size	0.480***	0.471***	0.453***	0.448***	0.464***	0.454***	0.468***	0.455***	0.459***	0.458***
	(0.020)	(0.022)	(0.029)	(0.031)	(0.031)	(0.028)	(0.032)	(0.031)	(0.028)	(0.031)
Leverage	0.104	0.103	0.315	0.328	0.264	0.312	0.233	0.255	0.315	0.254
	(0.128)	(0.128)	(0.172)	(0.178)	(0.183)	(0.170)	(0.183)	(0.182)	(0.168)	(0.181)
Market to book	0.027***	0.027***	0.031*	0.031*	0.033**	0.029*	0.028*	0.028*	0.027*	0.030*
	(0.008)	(0.008)	(0.012)	(0.012)	(0.012)	(0.012)	(0.012)	(0.012)	(0.012)	(0.012)
Return on assets (ROA)	0.002	0.002	0.002	0.002	0.001	0.002	0.001	0.002	0.002	0.001
	(0.002)	(0.002)	(0.003)	(0.003)	(0.003)	(0.003)	(0.003)	(0.003)	(0.003)	(0.003)
Board Characteristics										
Board size		0.195	0.316	0.308	0.295	0.286	0.283	0.271	0.273	0.285
		(0.124)	(0.173)	(0.171)	(0.170)	(0.170)	(0.173)	(0.173)	(0.167)	(0.173)
Chairman family		0.094	-0.001	0.005	-0.009	0.037	-0.011	0.004	0.025	0.004
		(0.050)	(0.070)	(0.071)	(0.071)	(0.066)	(0.072)	(0.071)	(0.066)	(0.071)
Independent directors		0.117	0.275	0.277	0.255	0.271	0.251	0.232	0.287	0.253
		(0.137)	(0.178)	(0.178)	(0.173)	(0.173)	(0.176)	(0.175)	(0.178)	(0.176)
Executive directors		-0.284	0.017	0.026	-0.030	0.157	0.006	-0.021	0.219	-0.009
		(0.232)	(0.341)	(0.342)	(0.336)	(0.332)	(0.336)	(0.336)	(0.332)	(0.338)
Ownership Structure										
Concentrated ownership			-0.081*	-0.082*	-0.048	-0.102**	-0.054	-0.057	0.014	-0.068*
			(0.032)	(0.033)	(0.026)	(0.033)	(0.033)	(0.033)	(0.049)	(0.032)
Managerial ownership			0.004	0.005	0.003		0.036*	0.004		0.005
			(0.003)	(0.003)	(0.003)		(0.015)	(0.003)		(0.003)
Institutional investor ownership			0.002	0.001			0.002	0.002		0.002
			(0.002)	(0.002)			(0.002)	(0.002)		(0.002)
Family ownership			0.004	0.005*	0.004		0.003	0.026		0.005*
			(0.002)	(0.002)	(0.002)		(0.002)	(0.014)		(0.002)
Foreign ownership				0.053			0.179*	0.182*		0.173*
				(0.078)			(0.087)	(0.087)		(0.087)
Government ownership					-0.004		-0.008*	-0.008*		-0.007*
					(0.003)		(0.003)	(0.003)		(0.003)
External ownership						0.004*			0.021***	
						(0.002)			(0.005)	
Concentrated*Managerial ownership							-0.004*			
							(0.002)			
Concentrated*Family ownership								-0.003		
								(0.002)		
Concentrated*External ownership									-0.003***	
									(0.001)	
Managerial*Family ownership										-0.000
										(0.000)
Industry dummy variables	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Year dummy variables	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Country dummy variables	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Number of observations	1,531	1,523	939	939	939	939	939	939	939	939

Table 4.13 Determinants of the choice between bonus and salary-Interaction variables

This table presents coefficient estimates for pooled OLS regressions estimating the relationship between corporate governance variables and performance. Industry, year and country dummy variables control for the macroeconomic conditions. Robust standard errors are reported in parenthesis. ***, ** and * represents significance levels at 1%, 5% and 10%, respectively. Definitions for all the variables are provided in Table 4.1.

	Model 1	Model 2	Model 3	Model 4	Model 5	Model 6	Model 7	Model 8	Model 9	Model 10
Financial and economic characteristics										
Firm size	0.013	0.009	0.023**	0.018	0.018	0.019*	0.015	0.015	0.020*	0.018
	(0.007)	(0.008)	(0.009)	(0.010)	(0.009)	(0.009)	(0.010)	(0.010)	(0.009)	(0.010)
Leverage	0.042	0.028	-0.057	-0.044	-0.050	-0.071	-0.032	-0.037	-0.072	-0.045
	(0.055)	(0.054)	(0.059)	(0.062)	(0.063)	(0.060)	(0.063)	(0.063)	(0.060)	(0.064)
Market to book	0.005	0.005*	0.012	0.012	0.011	0.011	0.012	0.010	0.011	0.012
	(0.003)	(0.002)	(0.007)	(0.007)	(0.007)	(0.007)	(0.007)	(0.007)	(0.007)	(0.007)
Return on assets (ROA)	0.000	0.000	0.000	0.000	0.000	0.000	0.000	0.000	0.000	0.000
	(0.001)	(0.001)	(0.001)	(0.001)	(0.001)	(0.001)	(0.001)	(0.001)	(0.001)	(0.001)
Board Characteristics										
Board size		0.051	0.006	-0.004	0.010	0.001	0.003	0.004	-0.007	0.001
		(0.040)	(0.053)	(0.054)	(0.054)	(0.053)	(0.056)	(0.055)	(0.054)	(0.056)
Chairman family		0.039*	0.012	0.016	0.015	0.025	0.017	0.015	0.025	0.015
		(0.019)	(0.025)	(0.025)	(0.024)	(0.024)	(0.025)	(0.025)	(0.024)	(0.025)
Independent directors		-0.096*	-0.086	-0.085	-0.082	-0.080	-0.083	-0.090	-0.081	-0.082
		(0.044)	(0.058)	(0.058)	(0.058)	(0.059)	(0.058)	(0.058)	(0.059)	(0.059)
Executive directors		0.124	0.198	0.193	0.220	0.268*	0.208	0.157	0.264*	0.200
		(0.094)	(0.116)	(0.115)	(0.116)	(0.110)	(0.121)	(0.119)	(0.111)	(0.120)
Ownership Structure										
Concentrated ownership			-0.001	-0.002	-0.015	-0.018	-0.005	0.003	-0.008	-0.005
			(0.012)	(0.013)	(0.009)	(0.012)	(0.013)	(0.013)	(0.018)	(0.013)
Managerial ownership			0.001	0.001	0.002*		-0.002	0.002*		0.002
			(0.001)	(0.001)	(0.001)		(0.004)	(0.001)		(0.001)
Institutional investor ownership			-0.001	-0.001			-0.001	-0.001		-0.001
			(0.001)	(0.001)			(0.001)	(0.001)		(0.001)
Family ownership			0.000	0.000	0.000		0.000	0.019*		0.001
			(0.001)	(0.001)	(0.001)		(0.001)	(0.008)		(0.001)
Foreign ownership				0.029			0.021	0.033		0.024
				(0.029)			(0.035)	(0.034)		(0.035)
Government ownership					0.001		0.001	0.000		0.000
					(0.001)		(0.001)	(0.001)		(0.001)
External ownership						0.001			0.002	
						(0.001)			(0.002)	
Concentrated*Managerial ownership							0.001			
							(0.000)			
Concentrated*Family ownership								-0.003*		
								(0.001)		
Concentrated*External ownership									-0.000	
									(0.000)	
Managerial*Family ownership										-0.000
										(0.000)
Industry dummy variables	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Year dummy variables	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Country dummy variables	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Number of observations	538	538	373	373	373	373	373	373	373	373

Table 4.14 Determinants of total executive compensation-Two-Stages Least Squares (2SLS)

This table presents coefficient estimates for Two-Stages Least Squares (2SLS) regressions estimating the relationship between corporate governance variables and performance. Industry, year and country dummy variables control for the macroeconomic conditions. Robust standard errors are reported in parenthesis. ***, ** and * represents significance levels at 1%, 5% and 10%, respectively. Definitions for all the variables are provided in Table 4.1.

	Model 1	Model 2	Model 3	Model 4	Model 5	Model 6
Financial and economic characteristics						
Firm size	0.492***	0.491***	0.481***	0.469***	0.477***	0.486***
	(0.030)	(0.033)	(0.043)	(0.041)	(0.041)	(0.045)
Leverage	0.176	0.162	0.245	0.282	0.264	0.216
	(0.181)	(0.187)	(0.282)	(0.270)	(0.262)	(0.305)
Market to book	0.006	0.006	0.008	0.008	0.012	0.007
	(0.022)	(0.022)	(0.034)	(0.034)	(0.037)	(0.034)
Return on assets	0.106	0.110	0.087	0.086	0.091	0.088
	(0.093)	(0.099)	(0.109)	(0.108)	(0.143)	(0.113)
Board Characteristics						
Board size		0.068	0.303	0.279	0.260	0.247
		(0.179)	(0.231)	(0.222)	(0.222)	(0.216)
Chairman family		0.084	-0.053	-0.038	-0.053	-0.035
		(0.078)	(0.116)	(0.110)	(0.121)	(0.125)
Independent directors		0.337	0.676	0.671	0.692	0.696
		(0.313)	(0.648)	(0.643)	(0.831)	(0.685)
Executive directors		-0.463	0.184	0.199	0.147	0.304
		(0.395)	(0.511)	(0.514)	(0.539)	(0.497)
Ownership Structure						
Concentrated ownership			-0.067	-0.072	-0.021	-0.081
			(0.042)	(0.041)	(0.047)	(0.044)
Managerial ownership			0.005	0.006	0.003	
			(0.004)	(0.004)	(0.004)	
Institutional investor ownership			0.004	0.004		
			(0.004)	(0.004)		
Family ownership			0.004	0.004	0.003	
			(0.003)	(0.003)	(0.003)	
Foreign ownership				0.134		
				(0.136)		
Government ownership					0.002	
					(0.009)	
External ownership						0.006
						(0.003)
Industry dummy variables	Yes	Yes	Yes	Yes	Yes	Yes
Year dummy variables	Yes	Yes	Yes	Yes	Yes	Yes
Country dummy variables	Yes	Yes	Yes	Yes	Yes	Yes
Number of observations	1,512	1,504	927	927	927	927

Table 4.15 Determinants of the choice between bonus and salary-Two-Stages Least Squares (2SLS)

This table presents coefficient estimates for Two-Stages Least Squares (2SLS) regressions estimating the relationship between corporate governance variables and performance. Industry, year and country dummy variables control for the macroeconomic conditions. Robust standard errors are reported in parenthesis. ***, ** and * represents significance levels at 1%, 5% and 10%, respectively. Definitions for all the variables are provided in Table 4.1.

	Model 1	Model 2	Model 3	Model 4	Model 5	Model 6
Financial and economic characteristics						
Firm size	0.015	0.013	0.028**	0.019	0.021*	0.024*
	(0.008)	(0.009)	(0.011)	(0.010)	(0.011)	(0.011)
Leverage	0.040	0.022	-0.083	-0.054	-0.062	-0.101
	(0.066)	(0.064)	(0.079)	(0.075)	(0.078)	(0.083)
Market to book	0.002	0.002	0.010	0.010	0.009	0.009
	(0.004)	(0.004)	(0.008)	(0.008)	(0.008)	(0.008)
Return on assets	0.014	0.012	0.011	0.010	0.011	0.011
	(0.012)	(0.011)	(0.011)	(0.010)	(0.011)	(0.011)
Board Characteristics						
Board size		0.018	-0.000	-0.019	0.003	-0.007
		(0.054)	(0.060)	(0.061)	(0.060)	(0.060)
Chairman family		0.047	0.013	0.020	0.016	0.024
		(0.024)	(0.027)	(0.027)	(0.027)	(0.026)
Independent directors		-0.048	-0.024	-0.032	-0.020	-0.017
		(0.072)	(0.097)	(0.093)	(0.096)	(0.099)
Executive directors		0.191	0.224	0.211	0.252	0.310*
		(0.128)	(0.135)	(0.128)	(0.136)	(0.133)
Ownership Structure						
Concentrated ownership			-0.003	-0.004	-0.014	-0.022
			(0.013)	(0.013)	(0.010)	(0.013)
Managerial ownership			0.002	0.002	0.002*	
			(0.001)	(0.001)	(0.001)	
Institutional investor ownership			-0.001	-0.001		
			(0.001)	(0.001)		
Family ownership			0.000	0.000	0.000	
			(0.001)	(0.001)	(0.001)	
Foreign ownership				0.048		
				(0.040)		
Government ownership					0.001	
					(0.001)	
External ownership						0.001
						(0.001)
Industry dummy variables	Yes	Yes	Yes	Yes	Yes	Yes
Year dummy variables	Yes	Yes	Yes	Yes	Yes	Yes
Country dummy variables	Yes	Yes	Yes	Yes	Yes	Yes
Number of observations	529	529	367	367	367	367

Chapter 5. Executive Compensation and Firm Performance in the GCC Countries

Abstract

This paper examines the relationship between executive compensation and firm performance in the Gulf Cooperation Council (GCC) countries. We collect compensation data from 295 non-financial companies from Kuwait, Oman, Qatar, Saudi Arabia and United Arab Emirates. We employ Tobin's Q to measure the firm performance. Total executive compensation, salary, bonus and the ratio of bonuses to total executive compensation are used as independent variables to proxy executive compensation. We utilize fixed and random effects panel data regression approach to estimate our models. We find that higher total executive compensation, adjusted for firm size, leads to better firm performance. On the other hand, we do not find any statistically significant relationship between Tobin's Q and the components of compensation, namely salary and bonus.

5.1 Introduction

There is an increasing interest on the ways executives are compensated and its affect on the firm performance. The relationship between executive compensation and firm performance has been subjected to several theoretical and empirical studies providing mixed results about this relationship. This study examines the relationship between executive compensation and firm performance in companies operating in the GCC countries. We use publicly available data (from company annual reports) on total compensation paid to the executives. To the best of our knowledge, this study is the first of its kind undertaken within the research setting of GCC region. GCC economies are generally characterised by the importance of family control, large population of expatriate executives, under-developed capital markets and relative absence of well-designed corporate governance mechanisms. These features make the GCC economic environment quite different from the Anglo-Saxon model and, therefore, investigating executive compensation within the GCC context has implications that go beyond specificities of such type of study conducted in other regions. Since the link between executive pay and firm performance represents one of the major constituents of managerial incentives for contributing to the firm growth and success, a closer look at this relationship is bound to provide much needed knowledge on the impact of executive pay on the performance of companies operating in the GCC countries.

Although the pay-performance link has been studied from different theoretical perspectives such as optimal contract theory (Alchian and Demsetz, 1972), tournament theory (Melton and Zorn, 2000), expectancy theory (Henemana and Schwab, 1972) and agency theory (Jensen and Meckling, 1976), most of the empirical studies have approached the issue from an agency theory perspective finding agency conflicts to be the key for the determination of the level of executive compensation. The agency theory attributes the agency conflicts arising of separation of ownership and control of widely-held companies to be the basis for providing the managers necessary incentives to act in the best interests of the shareholders and maximise their wealth. According to Jensen and Meckling (1976), agency conflicts may arise because of the existence of varied interests, differences in decision-making ability and process and information asymmetry between the owners (shareholders) and the agents (managers). In this context, Grossman and Hart (1983) refuted the optimal contract theory advocated by Alchian and Demsetz (1972)

which claims that optimal contracts making the executives to become the residual claimants of the profits and revenues of the firm might be able to encourage executives to work towards improved firm performance. Core et al. (1999) provided a new dimension to the pay-performance discourse by claiming that corporate governance variables are likely to have a major impact on the executive pay and thus on firm performance. The tournament theory propagated by Rosen (1986) argues that the salary differentials among the executives at different levels in the corporate hierarchy might be the tools to motivate the executives to improve the firm performance. The review of the previous literature as a part of this study considers the theoretical aspects of the pay-performance relationship.

The scope of the literature review includes analysing the findings of the empirical studies conducted earlier to the extent to which these findings apply to this study. It is observed that the empirical studies have provided mixed results on the relationship between the two variables and therefore a conclusive proof to the relationship appears to be lacking. For example, while Murphy (1985) found a strong relationship between executive compensation and firm performance, Jensen and Murphy (1990) could find only a weak relationship between the two. Murphy (1985, 1999) and Coughlan and Schmidt (1985) are some of the early researchers who provided empirical evidence on the relationship. Gibbons and Murphy (1990) considered firm size and its relationship to sensitivities in pay-performance and the findings proved an inverse relationship. Later findings of the study by Bebchuk and Fried (2004) empirically proved a weak association between CEO compensation and firm performance. Empirical studies conducted in the context of UK companies and the studies mostly provided evidence of a weak relationship (e.g. Gregg et al., 2005; Girma et al., 2007). In the research setting of Japan, Kato and Kubo (2006) found empirical evidence of a strong association between executive pay and firm performance of Japanese companies. The impact of corporate governance variables on the pay-performance relationship has also been the subject matter of many empirical studies (e.g. Marin et al., 2010; Banghoj et al., 2010; Brunello et al., 1997). Ownership structure is yet another variable that was empirically studied to assess its impact on pay-performance relationship (e.g. Edwards et al., 2007; Ang et al., 2000; Lin et al., 2011).

The relationship between executive compensation and firm performance in respect of companies operating in the GCC region has been understudied because of non-availability of comprehensive data. The corporate governance mechanisms that could

work in the context of GCC economies may differ substantially from those being applied in the Western and other advanced economies. However, there are only limited studies that focused on the impact of the governance variables on the pay-performance relationship. Aljifri and Moustafa (2007) suggested introducing suitable governance mechanisms in the region to improve firm performance. Hassan and Halbouni (2013) conducted an empirical study to identify that use of accounting based firm performance would be suitable to study the firm performance levels in respect of GCC companies. Al-Swidi et al. (2012) supported the view that because of the existence of unique culture and institutions GCC countries must have a different governance mechanism that would suit the economies. These studies have not explicitly studied the relationship between executive compensation and firm performance. In the absence of relevant literature in this respect, this study examined this relationship in the GCC companies.

We collect compensation data from 295 non-financial companies from Kuwait, Oman, Qatar, Saudi Arabia and United Arab Emirates. We use Tobin's Q to measure the firm performance and total executive compensation, salary, bonus and the ratio of bonuses to total executive compensation as independent variables to proxy executive compensation. We utilize fixed and random effects panel data regression approach to estimate our models. A set of variables controlling for other corporate governance indicators, firm financial characteristics and macroeconomic environment is also employed in the modeling. The findings of this study, when generalised, are expected to shed some light to the executive compensation patterns and policies of GCC companies. Implication of the findings may be used by the companies to review the impact of the relationship of executive pay with their respective performance.

Overall, we find that higher total executive compensation, adjusted for firm size, leads to better firm performance. On the other hand, we do not find any significant relationship between the components of compensation (salary and bonus) and performance. We interpret the findings of this study to point out that specific GCC economic environment and features peculiar to this region has more impact on the firm performance rather than the executive compensation. In selected models we find that total executive compensation to sales provided results showing a negative and significant relationship between pay and performance. While any increase in the size of executive compensation in relation to total assets might increase the Tobin's Q, same result cannot be expected in the Tobin's with

an increase in executive pay in relation to sales. This may be because the owners might consider the increase in the assets value as more tangible business performance than an increase in the sales and accordingly they might decide to compensate the executives more whenever they observe an increase in the total assets of the company. Nevertheless, in one of the random effect regression models, we find a positive and a significant coefficient between lagged of total executive compensation to total assets and firm performance. Therefore, it is argued that when the compensation figures are scald with firm size represented by total assets, the empirical results would become meaningful to assess the relationship between executive pay and performance in the GCC firms.

The paper is presented as follows: Section 5.2 contains a detailed review of the previous literature available on the topic. The literature review was undertaken to augment the theoretical knowledge on the research topic so that the empirical findings of this study can be related to the theoretical foundations laid down through the literature review. The methodology adopted for conducting the research is explained in Section 5.3 with a description of the variables considered for the study. The empirical findings and discussion on such findings form part of Section 5.4. Section 5.5 concludes the report on the research summarising the findings and detailing the limitations subject to which the study was to be conducted. Few recommendations for further research on the topic are also included in Section 5.5.

5.2 Literature Review

5.2.1 Theoretical Background

The relationship between the executive compensation and firm performance has been the focus of many previously conducted research studies. The academic literature has used tournament theory (Melton and Zorn, 2000), expectancy theory (Henemana and Schwab 1972) and agency theory including other socio-psychological factors in explaining the process of setting the managerial compensation. Among these theories agency theory has been widely used by the researchers in their studies examining the association between executive compensation and firm performance.

From an agency theory perspective, executive compensation linked to performance is most likely to provide incentives to executives to act in the best interests of the shareholders (Jensen and Meckling, 1976; Fama and Jensen, 1983). Agency theory which forms the basis for analysis of the relationship between management remuneration and firm performance is one of the dominant theoretical approaches used in the accounting literature. According to agency theory, separation of ownership and control creates agency conflicts. The agency conflicts are characterised by the existence of varied interests, differences in the level of risks that firms can take, differences in decision frontiers, and information asymmetry between the shareholders (principal) and managers (agent) (Jensen and Meckling, 1976). Because of the presence of diverging interests of the principal and agent the agency theory predicts that the executives who enjoy an information advantage are likely to act in their own interests instead of meeting that of the principal. The agency theory predicts that since shareholders might not be able to observe the actions of the mangers entirely, firms will evolve a compensation policy that would provide the managers necessary incentive to implement such actions that will work to maximise the shareholders' wealth.

The principal-agent conflict highlights the potential dangers of a divorce of ownership from control where senior management and executives engage in behaviour that maximises personal welfare at the expense of the firm. Jensen and Meckling (1976) argue that moral hazardous behaviour can be limited by deriving strategies which control the

activities of management whilst motivating them to align their interests with those of shareholders. During the 1990s, financial and economic theories were proposed, suggesting that executive compensation should be linked to financial performance as a means of motivating top executives and ensuring that their interests are aligned with maximising shareholder value. Studies devoted to empirically testing the causal relationship between different components of executive compensation and measures of financial performance revealed mixed results (Conyon, 2006).

Designing executive compensation to match firm performance gave rise to the optimal contract theory by Alchian and Demsetz (1972) who argued that employers should be residual claimants of the firm's profits and revenues in order to provide them with an incentive to improve firm performance. However, as argued by Grossman and Hart (1983), it is not easy to determine the optimal contract as this can vary depending on the characteristics of the corporation. Moreover, simple rules of mathematics prove that there may be multiple optimal contracts, making it difficult for the firm to choose.

In opposition to the contract theory, Core et al. (1999) argued that variations in senior executive pays were associated with corporate governance variables and not firm performance. The authors suggested that CEOs with abnormally high pays were the result of managerial entrenchment and poor governance structures that enabled executives to earn high pays despite no evidence of high firm performance. Similarly, Anabtawi (2005) argued that boards dependent on shareholders as opposed to managers would yield a positive and significant causal link between executive compensation and firm performance whilst managerial entrenchment or boards being captured by CEOs would yield a weak link.

In addition to incorporating corporate governance to determine the impact on the relationship between pay and performance, Chambers (2009) highlighted the practical hurdles in implementing the optimal contract theory. The author argued that rewarding executives on work or effort is difficult when the effort itself is unobservable or difficult to measure. Furthermore, linking pay and bonuses to firm performance may result in top executives adopting a myopic view of profit maximisation at the cost of long-term sustainable growth.

Despite theoretical limitations of the optimal contract theory, there is substantial evidence that firms choose to link the pay of senior executives with growth in firm profits or sales as argued by Hannes (2010). Although this may appear to be a successful strategy in motivating managers, it has also led to a rapid increase in risk taking and moral hazard. In particular, the author suggested that with the advent of globalisation, executive compensation has become more linked to stock options as compared to paying a fixed salary with cash bonus. In 1985, stock options formed 8 per cent of average CEO compensation increasing to 94 per cent by 1999. Companies believed that this would motivate executives to maximise firm value. However, this not only led to a surge in fraudulent practices, but also encouraged senior management to maximise short-term profit whilst exposing firms to the risk of long-term bankruptcy.

In contrast to the optimal contract theory, Rosen (1986) proposed the tournament theory arguing that salaries and bonuses were designed to motivate executives and encourage competition by increasing the wage spreads between employees at different levels of the corporate hierarchy. According to this theory, an increase in executive pay is not based on a rise in firm performance, but rather a promotion to a higher level of the corporate hierarchy. Anabtawi (2005) argues that tournament theory can help explain the differences in levels of executive compensation as well as help structure executive compensation.

5.2.2 Empirical Evidence

There has been a steady stream of empirical studies conducted on the relationship between executive compensation and firm performance since the study conducted by Roberts (1956). Murphy (1985), Jensen and Murphy (1990) and Hall and Liebman (1998) are some of the earlier researchers who focused on this topic. Murphy (1985) found a strong relationship between the two variables. Jensen and Murphy (1990) could find only a weak relationship between executive pay and corporate performance. The work of Jensen and Murphy (1990) led to significant increase in the inclusion of stock options in executive compensation packages in order to strengthen the relationship between pay and performance. During late 1990s Hall and Liebman (1998) found a stronger relationship

between executive pay and performance as compared to that reported by Jensen and Murphy (1990).

In the context of United States, prior to 1980, few earlier studies reported their findings on executive compensation (e.g. Roberts, 1956; Baumol, 1959; and Lewellen and Huntsman, 1970). Subsequently, Murphy (1985), Coughlan and Schmidt, (1985) and Murphy (1999) provided notable evidence on the relationship of the two variables. All these studies reported a strong relationship between the variables. Gerhart and Milkovich (1990) found evidence to prove the structure of pay in the form of bonuses and long-term incentives to have a strong association with better financial performance of companies. Gibbons and Murphy (1990) studied the relationship between firm size and sensitivities of pay-performance to report an inverse relationship among these variables. The findings of the study by Murphy (1999) also support the negative association between firm size and pay-performance sensitivities. Bebchuk and Fried (2004) report a weak link between CEO compensation and firm performance.

The empirical literature on the impact of executive compensation in the UK is rather limited as compared to the US empirical literature. For example, Girma et al. (2007) focused on the effect of Cadbury Committee reforms on executive pay by considering longitudinal data in respect samples of UK companies and reported a rather weak relationship between executive compensation and company performance over the period 1981-1996. Gregg et al. (2005) also reported a weak association between the variables. Gregg et al. (2012) focused on the relationship between firm performance and executive cash compensation in the large UK financial services firms and found that the cash-plus-bonus pay performance sensitivity in respect of firms operating in the industry is comparable to other industries with no significant variation on the higher side. Ozkan (2007) studied the impact of corporate governance mechanism for a sample of 414 UK companies for the year 2003 and reported an insignificant effect of firm performance on CEO compensation. However, this study suffered from the limitation of the data being related to one year only. For a recent period of 1999-2005 Ozkan (2011) found no association between the variables for UK companies. Thus evidence from the empirical studies in the context of UK exhibits a weak to moderate relationship between executive compensation and firm performance.

A number of empirical studies have reported on the relationship between stock options as a component of executive pay and its impact on firm performance. For instance, Yermack (1995) studied the effect of stock options in respect of 792 large firms and found a strong association of this component of executive pay with the performance of sample companies and the study related to the period 1984 to 1991. Empirical study by Mehran (1995) on 153 manufacturing firm for the period 1979 and 1980 provided evidence to prove that stock options had a significant impact on firm performance and reported that both percentage equity held by managers and percentage of manager compensation that was equity based had a positive causal relationship with firm performance.

Empirical studies have also been conducted to examine the relationship between executive compensation and firm performance in the context of emerging economies. For example, Kato and Long (2005) used comprehensive accounting and financial data in respect of Chinese firms and found statistically significant relationship between the variables. The study also found significant impact of ownership structure on pay-performance in the case of Chinese listed firms. In this context, Firth et al. (2007) found insignificant relationship between ownership structure and managerial pay in the case of Chinese state-owned companies. Pan et al. (2009) report a positive association between executive pay and firm performance in cases where there is equity-based compensation offered to the top executives. Li (2010) finds the negative impact of a dysfunctional governance system on firm performance and at the same time providing for excessive compensation to executives. Conyon and He (2011) examined the executive pay in Chinese companies and provided evidence for a positive association between executive pay and corporate governance. The study found that firms having more independent directors exhibit stronger relationship between pay and performance. Although there are not much studies in the Indian setting, Kakani and Ray (2002) observe no significant relationship between CEO pay and firm performance of Indian companies. Ghosh (2003) found a positive relationship between the variables and high pay-performance sensitivity in the case of smaller firms.

Fyre (2004) used Tobin's Q as the measure and found a strong effect of equity-based stock options on firm performance during 1992-1994 in respect of 121 in the United States studied by them. Murphy (1999) supports the finding that stock options have a direct and significant effect on firm performance in the context of United States. Similar

findings of a strong and positive association between stock options in the executive compensation and firm performance are reported by Fung et al. (2001) in China and Matsunaga and Park (2001) in the US. In the Japanese context, Kato and Kubo (2006) found evidence to show a strong relationship between pay and performance of Japanese firms. However, negative stock returns are likely to have twice the effect on firm performance as compared to positive stock returns when stock options are made a component of executive pay (Leone et al., 2006). Burns and Kedia (2006) argue that linking executive pay with stock options gives executives a greater incentive to misreport financial statements. The authors claim that stock options help to increase the complexity of executive pay in order to reduce the risk of misreporting if at all caught by authorities.

5.2.3 Corporate Governance and Executive Compensation

A substantial portion of the literature is dedicated to examining the impact of governance variables on the relationship between executive compensation and firm performance. As explained by the agency theory, the purpose of linking executive salaries and bonuses to firm performance is to reduce moral hazard and ensure that the interests of shareholders are protected. Studies examining governance variables provide mixed results with some arguing that good governance complements performance linked pay whilst others argue in favour of a substituting effect.

Economic theory proposes that the principle agent conflict increases with the separation of ownership from control necessitating firms to incur agency costs in order to monitor the behaviour of senior executives and management (Jensen and Meckling, 1976). Firms that do not institute proper governance mechanisms are most likely to induce managers to pursue their personal goals leading to misalignment of interests of the managers and shareholders leading to the failure of the optimal contract theory. In this regard, Marin et al. (2010), on their investigation of 120 non-financial Spanish firms between 2004 and 2006, argued that the pay-performance link breaks down at higher levels of executive pay as governance structures become weak with firm expansion. The study revealed a positive association between top managers' pay and firm performance at low levels of compensation with significant reversal at high levels of compensation. The authors argue that there is evidence in support of the agency theory at low levels of manager

compensation with earnings being used as a means of supervising managers and aligning interests to those of shareholders. However, with higher management earnings, the supervisory system fails and managers have greater discretion to pursue their own personal gains.

Similar results confirming the significance of governance in complementing agency theory has been found by Banghoj et al. (2010). The authors examined the impact of board size and ownership structure on the pay-performance relationship investigating 500 Danish firms to show that both board size and ownership structure helped to determine executive compensation in addition to other personal attributes of top managers. However, the findings were contrary to results found from other developed countries as the study reported an insignificant relationship between firm performance and executive compensation primarily due to the fact that performance related pay is not common in the private sector of Denmark. According to Brunello et al. (1997), the corporate governance mechanisms and its impact on pay-performance sensitivity in countries like Italy are found to be different from other Western nations primarily because of the pre-dominance of family owned businesses. In such countries firms have weak governance structures with less accountability and transparency.

Brunello et al. (1997) examined the pay-performance link in respect of 74 private sector firms in Italy to assess the impact of family owned businesses on the pay-performance link. In the first instance the study focused on the relationship between firm performance and executive pay for top and middle managers regardless of governance and found a significant and positive causal relationship between both variables. Secondly, the study hypothesised that poor governance structures and low bank monitoring suggested that pay-performance link within such firms should be less than their Anglo-Saxon and German-Japanese counterparts. And the findings confirmed that the relationship between firm performance and manager pay was more sensitive for foreign firms than domestic counterparts.

A similar study was conducted by Gigliotti (2013) examining 145 Italian companies that were listed on the Milan stock exchange to assess the association between the remuneration of top managers and firm performance. The findings of this study were contrary to those of Brunello et al. (1997). Gigliotti (2013) found an absence of

association between managers' pay and firm performance. The author argued that Italian firms adopt other measures to motivate and monitor managers as a means of countering moral hazard instead of pay-for performance. In addition, the author also found a strong link between firm size and managers' pay. Although the rise in pay may compensate for additional risk, it suggests that managers might be motivated to indulge in moral hazardous behaviour to increase firm size over the short run at the expense of long term sustainable profits.

In addition to board size and ownership structure, economic theory argues that good corporate governance requires a high proportion of outside directors that cannot be captured by CEOs and will monitor the activities of management effectively (Weisbach, 1987). This can also limit moral hazard. In testing this theory, Kren and Kerr (1997) analysed the annual statements for 268 firms listed on the Fortune 500 for the period 1987 and 1989 to determine the impact of outside directors and board shareholdings on the pay-performance link for top executives. The results revealed that firms with high board ownership had a greater link between executive compensation and firm performance. The authors argued that increased ownership in the firm provided an incentive to executives and directors to increase effort and improve firm performance complementing optimal contract theory. However, in contradiction to theory, the authors did not find evidence that firms with a large number of outside directors had a strong link between executive compensation and firm performance. The authors suggested that perhaps outside directors were less willing to monitor and control top executives by linking their pay to outcome.

Globalisation and the increasing role of institutional investors and financial institutions as stakeholders suggest a possibility that such institutions may provide an effective monitoring mechanism that affects the extent to which managers' pay needs to be associated with performance to limit the principle-agent conflict. This could imply a substituting effect on agency theory suggesting that banks and large institutional investors are inclined to monitor the behaviour of management and ensure that shareholder interests are being fulfilled. In such a scenario, there may not be a need to link pay with performance (Ang et al., 2000). For example, Edwards et al. (2007) investigated 271 non-financial German listed firms between 1989 and 1993 to determine the impact of concentrated ownership on the link between executive compensation and firm performance. The results of the study revealed an insignificant effect of concentrated

ownership except when the largest owner was a German financial institution. In that scenario, the link between executive compensation and firm performance was almost negligible. The author explained the result by arguing that financial institutions provide a strong governance mechanism that monitors the behaviour of executives and acts as a substitute to performance related pay. Therefore, in the case of Germany, there is no need to provide incentives such as pay linked to performance to mitigate agency problems if financial institutions have a large ownership in the company.

Similar results were found from Lin et al. (2011) who analysed a sample of 1175 high tech Taiwanese firms for the period spanning 2004 to 2006 with results suggesting that the direct control of institutional investors substituted the role of executive compensation as a means of reducing the agency problem. Therefore, firms with a high proportion of institutional investors faced a weaker link between executive compensation and firm performance than firms with a low proportion of institutional investors.

In contrast, Colpan and Yoshikawa (2012) found opposing evidence when examining a group of 153 large publicly traded Japanese firms between 1997 and 2007. Results suggested that the inclusion of corporate appointed directors and foreign ownership complemented executive compensation increasing the link between bonus and firm growth. In addition, bank appointed directors strengthened both the link between firm growth and bonus as well as firm profits and bonus. This suggests that incurring debt and including banks as stakeholders motivates managers to further improve firm performance in order to raise individual pay.

5.2.4 Executive Compensation and Firm Performance in GCC

Despite the importance of good governance structures for firm performance and foreign direct investment, there are still comparatively fewer studies that examine governance structures in GCC countries than other parts of the world. In addition, due to non-availability of data, limited studies have investigated the relationship between executive compensation and firm performance. Acknowledging the role of governance in mitigating the principle-agent conflict and the possible impact it can have on the link between executive pay and firm performance, this section highlights some of the important

findings regarding corporate governance in GCC economies. Empirical studies examining the relationship between governance and firm performance in selected GCC countries are also highlighted.

Acknowledging the strong role of culture in the GCC, Islam plays a prominent role in governing the actions and decisions of individuals in the corporate and non-corporate sector of Arab countries as argued by Baydoun et al. (2013). Even though clear principles of governance may not exist, the authors believe that religion and culture impose an indirect monitoring and control system on executives and all employees which limit moral hazard. Moreover, the majority of institutions in the GCC are not as advanced or mature as compared to those in the West with businesses being primarily family owned. As a result, ownership is largely in the hands of a few shareholders. For businesses that are not family owned, the State has significant control over the firm. Therefore, the monitoring role prescribed to non-executive directors is absent in Middle Eastern firms with a high owner concentration ratio. Firms willing to expand will either offer increased shares to existing shareholders or will send personal invitations to influential and wealthy families. This coincides with Shleifer and Vishny's (1997) classification on governance systems, with countries in the GCC being less dependent on the market system and more reliant on a highly concentrated ownership structure, similar to firms in Germany and Spain.

However, authors such as Aljifri and Moustafa (2007) argue that rapid globalisation and foreign direct investment in many of the GCC countries is forcing them to adopt governance practices that are aligned with those in the US or UK. Similarly, influx of foreign expatriates into the country suggests that obstacles can be minimised if similar corporate governance structures are used in the Middle East. Focusing on the UAE, the authors examined the role of governance variables in determining firm performance as measured by Tobin Q. The results revealed that the same governance variables known to be significant determinants of firm performance in the West were found to be insignificant in UAE including debt ratio and pay-out dividends ratio. Although the author did not test for executive compensation, the difference in corporate governance structures between UAE and US or UK can imply that perhaps linking pay to performance may not be a successful means of monitoring and motivating management. However, as the economy continues to build its capital market and implement international corporate governance

codes, there is a possibility that implementing optimal contract theory could yield positive results in the future.

Although the study by Aljifri and Moustafa (2007) led to some important conclusions regarding the divergence between current governance practices in the UAE and those implemented in the US. Hassan and Halbouni (2013) argue that the use of accounting based firm performance can yield different results from market based firm performance as measured by Tobin Q. Repeating the earlier study by Aljifri and Moustafa (2007), the authors collected sample of 95 UAE firms and obtained market based measures of firm performance using Tobin Q in addition to accounting based measures of firm performance that included accounting measures of Return on Equity and Return on Assets. Governance variables included CEO duality, voluntary disclosure and board size. All three variables were found to be insignificant determinants of market based measure of firm performance whilst being significant determinants of accounting based measures of firm performance. Therefore, in contrast to conclusions drawn from Aljifri and Moustafa (2007), the results from the study by Hassan and Halbouni (2013) suggest that the same governance principles in the US and UK can be found to be applicable in the UAE. Moreover, if governance principles are the same, this could suggest that agency costs can be reduced by linking pay to performance.

Despite acknowledging the need to conform to international governance standards in order to promote influx of foreign capital, Al-Swidi et al. (2012) argue that GCC countries have a unique set of infrastructure, culture and institutions which necessitate a code of governance that is suitable to them. At present, governance is weak and foreign expatriates complain that agency costs are high and monitoring mechanisms are not effective resulting in managerial entrenchment. Managers' interests are not aligned with those of shareholders and this affects firm performance. However, the authors argue that this does not imply blindly adopting practices in the West. Examining the impact of a set of governance variables, the authors argued that CEO duality was found to have significant and positive effect on firm performance whilst board size and composition were insignificant. Therefore, contrary to most studies in the US (e.g. Lawrence and Stapledon, 1999; Booth et al., 2002) which suggest that independent directors can help monitor executives and reduce agency costs; independent directors in Kuwaiti firms do not effectively monitor management. The authors argue that differences in culture and

the predominance of family businesses may imply that a unique code of governance is more suitable for the country.

Economic theory would suggest that firms run by family businesses with a high owner concentration ratio should not suffer from the agency problem since there is no separation of ownership from control. Board of directors are primarily controlled by large shareholders that include families and relatives. This would imply that top executives and managers in such firms are motivated enough to maximise firm value without having pay linked to performance (Baydoun et al., 2013). However, as argued by Gavin (2010) there are incidences where large family owned businesses have faced insolvency due to governance issues that include low transparency and accountability, secrecy and increased reliance on personal relationships. Therefore, the author argues that a high concentration ratio results in poor governance despite the fact that managers and owners are the same.

To investigate whether or not concentrated ownership that stems from family owned businesses has any effect on agency costs and firm performance, Al-Shammari and Al-Sultan (2009) examined the impact of a set of governance variables on firm performance for a group of listed firms in Kuwait. In particular, the authors examined the role of ownership concentration arguing that firms in Kuwait are predominantly family owned. All listed firms in the sample had three main groups of shareholders that included government agencies, dominant family members and institutional investors. Surprisingly, the results revealed that board size and CEO duality were positively associated with firm performance whilst ownership concentration was negatively associated with firm performance. Therefore, despite a predominance of family owned businesses, concentrated ownership is not an effective monitoring mechanism that can reduce agency costs. This reinforces the idea that perhaps the same underlying governance principles in the US and UK apply to the GCC countries. Investigating the role of optimal contract theory in such economies may yield important conclusions regarding its ability to align managerial interests with those of shareholders.

In an attempt to focus on managerial influence and pay in the GCC countries, the inclusion of CEO compensation and managerial entrenchment in regression models to investigate the impact on firm performance has yielded inconclusive results. For example,

Al-Matar et al. (2014) examined the impact of governance variables on firm performance for 81 non-financial firms in Oman between 2011 and 2012. The authors included CEO compensation with results revealing a positive, but insignificant relationship between compensation and firm performance. Therefore, the predominance of family-owned businesses and particular culture within Oman and neighbouring GCC countries may imply that performance related pay will not be successful in motivating executives.

In contrast, Hasan et al. (2014) examined 1921 non-financial firms from Bahrain, Kuwait, Oman, Saudi Arabia, Tunisia, Egypt, Israel and Morocco with results confirming a positive and significant causal relationship between low managerial entrenchment and firm value. Since family owned firms in the Middle East are known to suffer from high entrenchment the results imply that performance related pay might yield a significant relationship in such firms.

In conclusion, despite the rising number of studies that examine corporate governance in GCC countries and their influence on firm performance, the results have been inconclusive. Although some authors argue that empirical results reinforce the idea that principles of governance in the GCC countries are similar to international standards, others suggest that economies in the region have a distinct institutional structure and culture that requires a different code of governance. The extent of the difference between governance in the GCC economies and international governance standards will have an effect on whether or not linking executive pay to firm performance can help to reduce agency costs in the Middle East.

5.3 Methodology and Data

In this section a description of the data used for the study, the empirical methodology and the definitions of the variables are presented. The study followed a causal research design for investigating the relationship between executive compensation and firm performance in the GCC countries. The sample population for the study includes listed public companies operating in the GCC countries in respect of which the data relating to executive remuneration is available in the public documents like annual reports.

5.3.1 Empirical Model

We contribute to the above mentioned literature on the impact of executive compensation on firm performance in the GCC countries. This study uses Tobin's Q to measure firm performance. This is in line with earlier studies which employ the Tobin's Q as dependent variables (e.g. Mehran 1995; Ghosh 2003; Fyre 2004). The independent variables include total executive compensation and its components as salary and bonus and the choice between bonuses and salaries. This study uses both fixed effects and random effects regression approach to analyse the panel data collected in respect of GCC companies. This approach enabled the exercise of control over unobservable characteristics of GCC firms.

Considering the lack of previous research studies in the GCC context, we believe that this empirical analysis could as well be considered as the first empirical benchmark in studying the relationship between executive pay and firm performance in GCC companies.

We estimate the following models to examine the relationship between executive compensation and firm performance in GCC countries. First we start by looking at the relationship between total executive compensation and firm performance. This model is given below:

$$Performance_{i,t} = \beta_0 + \beta_1 Total\ executive\ compensation_{i,t}$$
$$+ \beta_2 Concentrated\ Ownership_{i,t} + \beta_3 Managerial\ Ownership_{i,t}$$
$$+ \beta_4 Foreign\ Ownership_{i,t} + \beta_5 Family\ Ownership_{i,t}$$
$$+ \beta_6 Government\ Ownership_{i,t} + \beta_7 External\ Ownership_{i,t}$$
$$+ \beta_8 Board\ Size_{i,t} + \beta_9 Chairman\ family_{i,t}$$
$$+ \beta_{10} Independent\ Directorss_{i,t} + \beta_{11} Executive\ Directors_{i,t}$$
$$+ \beta_{12} Firm\ Size_{i,t} + \beta_{13} Leverage_{i,t} + \sum_{y=1}^{Y-1} \beta_y \times Year_{i,y}$$
$$+ \sum_{j=1}^{J-1} \beta_j \times Industry_{i,j} + \sum_{c=1}^{C-1} \beta_c \times Country_{i,c} + e_{i,t,y,j,c}$$

In the second stage of our analysis we separate the total executive compensation to its components. We then look at the relationship between salary and firm performance. This model is given below:

$$Performance_{i,t} = \beta_0 + \beta_1 Salary_{i,t} + \beta_2 Concentrated\ Ownership_{i,t}$$
$$+ \beta_3 Managerial\ Ownership_{i,t} + \beta_4 Foreign\ Ownership_{i,t}$$
$$+ \beta_5 Family\ Ownership_{i,t} + \beta_6 Government\ Ownership_{i,t}$$
$$+ \beta_7 External\ Ownership_{i,t} + \beta_8 Board\ Size_{i,t}$$
$$+ \beta_9 Chairman\ family_{i,t} + \beta_{10} Independent\ Directorss_{i,t}$$
$$+ \beta_{11} Executive\ Directors_{i,t} + \beta_{12} Firm\ Size_{i,t} + \beta_{13} Leverage_{i,t}$$
$$+ \sum_{y=1}^{Y-1} \beta_y \times Year_{i,y} + \sum_{j=1}^{J-1} \beta_j \times Industry_{i,j} + \sum_{c=1}^{C-1} \beta_c \times Country_{i,c}$$
$$+ e_{i,t,y,j,c}$$

We also look at the relationship between bonus and firm performance. This model is given below:

$$\begin{aligned}
Performance_{i,t} = \ & \beta_0 + \beta_1 Bonus_{i,t} + \beta_2 Concentrated\ Ownership_{i,t} \\
& + \beta_3 Managerial\ Ownership_{i,t} + \beta_4 Foreign\ Ownership_{i,t} \\
& + \beta_5 Family\ Ownership_{i,t} + \beta_6 Government\ Ownership_{i,t} \\
& + \beta_7 External\ Ownership_{i,t} + \beta_8 Board\ Size_{i,t} \\
& + \beta_9 Chairman\ family_{i,t} + \beta_{10} Independent\ Directorss_{i,t} \\
& + \beta_{11} Executive\ Directors_{i,t} + \beta_{12} Firm\ Size_{i,t} + \beta_{13} Leverage_{i,t} \\
& + \sum_{y=1}^{Y-1} \beta_y \times Year_{i,y} + \sum_{j=1}^{J-1} \beta_j \times Industry_{i,j} + \sum_{c=1}^{C-1} \beta_c \times Country_{i,c} \\
& + e_{i,t,y,j,c}
\end{aligned}$$

Subsequently, we look at the relationship between the ratio of bonus to total executive compensation and firm performance. This model is given below:

$$\begin{aligned}
Performance_{i,t} = \ & \beta_0 + \beta_1 Bonus\ to\ total\ compensation_{i,t} \\
& + \beta_2 Concentrated\ Ownership_{i,t} + \beta_3 Managerial\ Ownership_{i,t} \\
& + \beta_4 Foreign\ Ownership_{i,t} + \beta_5 Family\ Ownership_{i,t} \\
& + \beta_6 Government\ Ownership_{i,t} + \beta_7 External\ Ownership_{i,t} \\
& + \beta_8 Board\ Size_{i,t} + \beta_9 Chairman\ family_{i,t} \\
& + \beta_{10} Independent\ Directorss_{i,t} + \beta_{11} Executive\ Directors_{i,t} \\
& + \beta_{12} Firm\ Size_{i,t} + \beta_{13} Leverage_{i,t} + \sum_{y=1}^{Y-1} \beta_y \times Year_{i,y} \\
& + \sum_{j=1}^{J-1} \beta_j \times Industry_{i,j} + \sum_{c=1}^{C-1} \beta_c \times Country_{i,c} + e_{i,t,y,j,c}
\end{aligned}$$

Table 5.1 presents the definitions of all variables used for each category. There are thirteen independent variables in this study, divided into four groups. The first group is compensation structure including total executive compensation, salary, bonus and the ratio of bonuses to total executive compensation. The second group is board characteristics which includes board size, chairman family, independent directors and executive directors. The third group is financial characteristics including firm size and leverage. The last group is ownership structures which include concentrated ownership,

managerial ownership, foreign ownership, family ownership, government ownership and external ownership.

Table 5.1 Definitions of dependent and independent variables

This table reports the definition of the variables that are used in the study. For ownership variables we do not report the values if shares owned is less than 5 per cent. All the variables are measured at the end of each year. Compensation figures are reported in US Dollars. Sources: Thomson one.com, Datastream and annual reports of the companies.

Performance measures	
Tobin's Q	The ratio of the book value of total assets minus the book value of equity plus the market value of equity to the book value of assets
Compensation Structure	
Total executive compensation	The annual cash compensation paid to top five executive directors in terms of salary and bonuses. Log of the variable is used
Salaries	The annual salary paid to top five executive directors. Log of the variable is used
Bonuses	The annual bonuses paid to top five executive directors. Log of the variable is used
Bonus to total compensation	The percentage of bonuses to total executive compensation
Total executive compensation to total assets	The annual cash compensation paid to top five executive directors in terms of salary and bonuses divided by total assets of the company
Total executive compensation to sales	The annual cash compensation paid to top five executive directors in terms of salary and bonuses divided by sales of the company
Salaries to total assets	The annual salary paid to top five executive directors divided by total assets of the company
Salaries to sales	The annual salary paid to top five executive directors divided by sales of the company
Bonuses to total assets	The annual bonuses paid to top five executive directors divided by total assets of the company
Bonuses to sales	The annual bonuses paid to top five executive directors divided by sales of the company
Board Characteristics	
Board size	The total number of directors on the board. Log of the variable is used
Executive directors	The number of executive directors divided by the board size
Independent directors	The number of independent directors divided by the board size
Chairman family	Equals to 1 if the chairman is a member of the family owning the company and 0 otherwise
Ownership Structure	
Managerial ownership	The percentage of shares owned by managerial (CEO and chairman) for shareholding of 5 per cent or more
Family ownership	The percentage of shares owned by family for shareholding of 5 per cent or more
Government ownership	The percentage of shares owned by local government for shareholding of 5 per cent or more
Foreign ownership	Is a dummy variable taking the value of 1 if foreign investors owned shares in the company and 0 otherwise
External ownership	The percentage of shares owned by outsiders. It equals to total ownership minus the total of managerial and family ownership for shareholding of 5 per cent or more
Concentrated ownership	The log of Herfindahl Index for measuring concentrated ownership. The Herfindahl index is defined as the sum of the squared sums of all owners shareholdings
Financial and economic characteristics	
Leverage	The ratio of total debt to total liabilities
Firm size	The natural logarithm of total assets
Sales	The gross sales and other operating revenue less discounts, returns and allowances. Log of the variable is used
Industry dummy variables	Each dummy variable equals to 1 for the specific industry reported and 0 otherwise. The industry classifications are Industrial, Services, Real estate and Building, Food and Beverage, Transport, Telecommunication and Utilities
Year dummy variables	Each dummy variable equals to 1 for the specific year variables (2006 to 2011) are reported and 0 otherwise
Country dummy variables	Each dummy variables equals to 1 for the specific country reported and 0 otherwise. The countries are Kuwait, Oman, Qatar, Saudi Arabia and United Arab Emirates

5.3.2 Data and Sources

The objective of the research design is to concentrate on the executive compensation of GCC countries' companies. Due to data availability our sample includes five countries from the GCC. These are Kuwait, Oman, Qatar, Saudi Arabia and United Arab Emirates. For example, Bahrain is characterised only by financial firms with no available data and, consequently not included in the study.

Our sample includes 295 listed firms for the period between 2006 and 2011. Financial firms such as banks and insurance companies were excluded from this study due to the unique nature of the sector and the inconsistency and variations in the calculations of Tobin's Q. The data is gathered from different sources, namely, Thomson one banker, Thomson.com, Datastream and annual reports. All of the board characteristics and compensation structure data used in this study were manually collected from the annual reports for all firms. Financial data is obtained from Thomson One Banker and Datastream. Ownership structure data is obtained from Thomson.com. However, it is important to mention that there are limitations to the data collection, in particular in relation to the distribution of salary and bonuses. In our sample 295 firms report the level of total compensation they give to their top executives. However, only 147 of these include the distribution of salary and bonuses within the total compensation. Also, some of annual reports are missing during the period of the study.

5.4   Results

5.4.1   Descriptive Statistics

The descriptive statistics for the variables used in the study are presented below in Table 5.2. It is observed that the mean of the total executive compensation is USD 2,078,261. Because of the large number of samples considered the minimum value for this variable is USD 3,683 and the maximum is USD 126,000,000. On a comparison with the total compensation paid to executives in China where the minimum average compensation was around USD 1200 and the maximum of USD 3,000,000, the executive compensation levels in the GCC region appears to be high (Buck et al., 2008). While the average executive compensation is USD 2,078,000, the average total compensation for the executives working in the companies listed in NASDAQ in the United States was found to be USD 31,090,000 (Abraham et al., 2014). Therefore it is inferred that the total executive compensation levels in the GCC countries is above the level of other developing countries but less than that prevailing in the United States. However, the fact that the total executive compensation in the United States includes stock options provided to the executives whereas the total compensation considered for this study includes the salary and bonus needs to be considered while comparing the levels of compensation.

We also provide the breakdown of executive compensation into its components of salary and bonus. It is worth to note again that this information is only available for 400 observations. Average salary paid to the top five executives is USD 1,169,695 while the average bonus is 598,143. We observe a larger variation in these variables. Looking at the firm characteristics, it can be observed that the firm size and sales has a mean value of 5.45 in the case of log of firm size and 4.18 in respect of log of sales. The descriptive statistics indicates that the mean value for leverage is 0.23.

Table 5.1 Descriptive statistics

This table reports descriptive statistics of the variables that are used in the study. For ownership variables we do not report the values if shares owned is less than 5 per cent. All the variables are measured at the end of each year. Sources: Thomson one.com, Datastream and annual reports of the companies. Definitions for all the variables are provided in Table 5.1.

Variable	Number of observations	Mean	Median	Std. Dev	Minimum	Maximum
Performance measures						
Tobin's Q	1014	1.77	1.69	1.15	0.15	12.90
Compensation Structure						
Total Executive Compensation	1014	2,078,261	6,651,991	806,432	3,683	126,000,000
Salaries	400	1,169,695	5,181,242	610,983	634	116,000,000
Bonuses	400	598,143	1,483,838	203,631	0.00	15,500,000
Bonus to total compensation	400	0.30	0.22	0.28	0.00	1.00
Firm Characteristics						
Firm size	1014	5.45	1.78	5.41	0.61	11.39
Sales	1014	4.18	2.50	3.78	-2.81	12.15
Leverage	1014	0.23	0.20	0.19	0.00	0.89
Ownership Structure						
Concentrated ownership	1014	6.27	1.37	6.27	1.75	9.21
Managerial ownership	1014	0.04	0.10	0.00	0.00	0.95
Foreign ownership	1014	0.28	0.45	0.00	0.00	1.00
Family ownership	1014	0.05	0.14	0.00	0.00	0.85
Government ownership	1014	0.06	0.15	0.00	0.00	0.81
External ownership	1014	0.45	0.24	0.45	0.02	1.00
Board Characteristics						
Board size	1014	7.27	1.89	7.00	3.00	13.00
Chairman family	1014	0.38	0.48	0.00	0.00	1.00
Independent directors	1014	0.78	0.25	0.86	0.00	1.00
Executive directors	1014	0.11	0.11	0.11	0.00	0.71

5.4.2 Results of the Regression Analysis

In this section, the empirical results from the econometric models shown in the previous section are presented. We run fixed and random effect estimations for our models and both results are presented.

In Table 5.3 and Table 5.4, we present the regression results for four models with total executive compensation, its components as salary and bonus and the ratio of bonus to total compensation (or the choice between bonus and salary) after controlling for corporate governance variables (e.g. ownership structure and board characteristics) and firm characteristics. Looking at the association between total executive compensation and Tobin's Q in Model 1 in Table 5.3, we do not find a significant relationship neither for fixed nor for random effect models. Similarly, the coefficients of salary, bonus, and bonus to total executive compensation in Models 1, 2 and 3 are not statistically significant. Thus

results in Table 5.4 do not provide evidence for any significant relationship between the total executive compensation and its components with Tobin's Q.

In Table 5.5 and Table 5.6 we present the results of our four main models using sales as an indicator of firm size (rather than the total assets). As above we do not find any significant relationship between any types of compensation set up and firm performance.

Table 5.2 Total executive compensation and Tobin's Q - the baseline model

This table presents coefficient estimates for fixed effects and random effects regressions estimating the relationship between corporate governance variables and performance using Tobin's Q as the dependent variable. Industry, year and country dummy variables control for the macroeconomic conditions. Robust standard errors are reported in parenthesis. ***, ** and * represents significance levels at 1%, 5% and 10%, respectively. Definitions for all the variables are provided in Table 5.1.

Independent Variable	Model 1	
	Fixed Effects	**Random Effects**
Compensation Structure		
Total executive compensation	0.061	0.021
	(0.054)	(0.042)
Firm Characteristics		
Firm size	-0.281	-0.122*
	(0.147)	(0.049)
Leverage	-1.501***	-1.364***
	(0.361)	(0.235)
Ownership Structure		
Concentrated ownership	0.019	-0.037
	(0.081)	(0.049)
Managerial ownership	0.053*	0.008
	(0.024)	(0.006)
Foreign ownership	0.178	0.099
	(0.245)	(0.138)
Family ownership	-0.062**	-0.012**
	(0.020)	(0.004)
Government ownership	0.007	0.002
	(0.013)	(0.005)
External ownership	0.001	0.005*
	(0.004)	(0.002)
Board Characteristics		
Board size	0.300	0.049
	(0.465)	(0.232)
Chairman family	-0.015	0.209
	(0.479)	(0.118)
Independent directors	-0.009	0.003
	(0.313)	(0.246)
Executive directors	0.024	0.524
	(0.885)	(0.507)
Industry dummy variables	Yes	Yes
Year dummy variables	Yes	Yes
Country dummy variables	Yes	Yes
Number of observations	1,014	1,014
Number of groups	295	295

Table 5.3 Compensation structure and Tobin's Q

This table presents coefficient estimates for fixed effects and random effects regressions estimating the relationship between corporate governance variables and performance using Tobin's Q as the dependent variable. Industry, year and country dummy variables control for the macroeconomic conditions. Robust standard errors are reported in parenthesis. ***, ** and * represents significance levels at 1%, 5% and 10%, respectively. See Table 5.1 for exact definitions of variables.

Independent Variable	Model 1 Fixed Effects	Model 1 Random Effects	Model 2 Fixed Effects	Model 2 Random Effects	Model 3 Fixed Effects	Model 3 Random Effects
Compensation Structure						
Salary	0.046	0.003				
	(0.064)	(0.035)				
Bonuses			-0.008	0.003		
			(0.016)	(0.014)		
Bonus to total compensation					-0.001	0.078
					(0.221)	(0.179)
Firm Characteristics						
Firm size	0.038	-0.021	0.060	-0.020	0.055	-0.022
	(0.167)	(0.049)	(0.166)	(0.048)	(0.169)	(0.048)
Leverage	0.214	-0.467	0.225	-0.467	0.214	-0.464
	(0.381)	(0.242)	(0.382)	(0.241)	(0.383)	(0.241)
Ownership Structure						
Concentrated ownership	-0.055	-0.080	-0.051	-0.080	-0.057	-0.079
	(0.100)	(0.052)	(0.101)	(0.052)	(0.101)	(0.052)
Managerial ownership	0.013	0.005	0.014	0.005	0.014	0.005
	(0.021)	(0.005)	(0.021)	(0.005)	(0.021)	(0.005)
Foreign ownership	0.133	0.020	0.150	0.018	0.140	0.017
	(0.147)	(0.113)	(0.148)	(0.114)	(0.147)	(0.114)
Family ownership	-0.012	-0.003	-0.012	-0.003	-0.013	-0.003
	(0.020)	(0.004)	(0.020)	(0.004)	(0.020)	(0.004)
Government ownership	0.006	0.004	0.007	0.004	0.006	0.004
	(0.009)	(0.004)	(0.009)	(0.004)	(0.009)	(0.004)
External ownership	0.000	0.003	-0.000	0.003	0.000	0.003
	(0.004)	(0.003)	(0.004)	(0.003)	(0.004)	(0.003)
Board Characteristics						
Board size	0.071	-0.016	0.071	-0.016	0.070	-0.017
	(0.287)	(0.204)	(0.287)	(0.203)	(0.288)	(0.203)
Chairman family		-0.053		-0.055		-0.056
		(0.124)		(0.123)		(0.123)
Independent directors	-0.031	0.012	-0.017	0.013	-0.020	0.019
	(0.185)	(0.157)	(0.185)	(0.157)	(0.185)	(0.157)
Executive directors	-0.155	0.353	-0.162	0.352	-0.140	0.350
	(0.679)	(0.438)	(0.680)	(0.437)	(0.680)	(0.437)
Industry dummy variables	Yes	Yes	Yes	Yes	Yes	Yes
Year dummy variables	Yes	Yes	Yes	Yes	Yes	Yes
Country dummy variables	Yes	Yes	Yes	Yes	Yes	Yes
Number of observations	400	400	400	400	400	400
Number of groups	147	147	147	147	147	147

Table 5.4 Total executive compensation and Tobin's Q with firm size measured as sales

This table presents coefficient estimates for fixed effects and random effects regressions estimating the relationship between corporate governance variables and performance using Tobin's Q as the dependent variable. Industry, year and country dummy variables control for the macroeconomic conditions. Robust standard errors are reported in parenthesis. ***, ** and * represents significance levels at 1%, 5% and 10%, respectively. Definitions for all the variables are provided in Table 5.1.

	Model 1	
	Fixed Effects	**Random Effects**
Compensation Structure		
Total executive compensation	0.006	0.005
	(0.060)	(0.046)
Firm Characteristics		
Sales	0.022	0.012
	(0.034)	(0.026)
Leverage	0.261	-0.518*
	(0.362)	(0.227)
Ownership Structure		
Concentrated ownership	-0.061	-0.080
	(0.097)	(0.052)
Managerial ownership	0.016	0.004
	(0.020)	(0.005)
Foreign ownership	0.143	0.001
	(0.147)	(0.111)
Family ownership	-0.014	-0.003
	(0.020)	(0.004)
Government ownership	0.006	0.003
	(0.009)	(0.004)
External ownership	0.000	0.003
	(0.004)	(0.003)
Board Characteristics		
Board size	0.080	-0.047
	(0.287)	(0.200)
Chairman family		-0.058
		(0.123)
Independent directors	-0.025	0.020
	(0.185)	(0.157)
Executive directors	-0.132	0.328
	(0.679)	(0.435)
Industry dummy variables	Yes	Yes
Year dummy variables	Yes	Yes
Country dummy variables	Yes	Yes
Number of observations	399	399
Number of groups	147	147

Table 5.5 Compensation structure and Tobin's Q with firm size measured as sales

This table presents coefficient estimates for fixed effects and random effects regressions estimating the relationship between corporate governance variables and performance using Tobin's Q as the dependent variable. Industry, year and country dummy variables control for the macroeconomic conditions. Robust standard errors are reported in parenthesis. ***, ** and * represents significance levels at 1%, 5% and 10%, respectively. Definitions for all the variables are provided in Table 5.1.

	Model 1		Model 2		Model 3	
	Fixed Effects	Random Effects	Fixed Effects	Random Effects	Fixed Effects	Random Effects
Compensation Structure						
Salary	0.048	-0.004				
	(0.064)	(0.035)				
Bonuses			-0.008	0.002		
			(0.016)	(0.014)		
Bonus to total compensation					0.006	0.061
					(0.218)	(0.179)
Firm Characteristics						
Sales	0.021	0.013	0.022	0.012	0.022	0.012
	(0.034)	(0.025)	(0.034)	(0.025)	(0.034)	(0.025)
Leverage	0.248	-0.510*	0.279	-0.515*	0.264	-0.515*
	(0.361)	(0.226)	(0.362)	(0.224)	(0.361)	(0.223)
Ownership Structure						
Concentrated ownership	-0.057	-0.081	-0.057	-0.081	-0.062	-0.080
	(0.097)	(0.052)	(0.097)	(0.052)	(0.097)	(0.052)
Managerial ownership	0.014	0.005	0.015	0.005	0.016	0.004
	(0.021)	(0.005)	(0.021)	(0.005)	(0.021)	(0.005)
Foreign ownership	0.136	0.003	0.153	0.001	0.144	-0.001
	(0.147)	(0.111)	(0.148)	(0.111)	(0.148)	(0.111)
Family ownership	-0.013	-0.003	-0.013	-0.003	-0.014	-0.003
	(0.020)	(0.004)	(0.020)	(0.004)	(0.020)	(0.004)
Government ownership	0.006	0.003	0.006	0.003	0.006	0.003
	(0.009)	(0.004)	(0.009)	(0.004)	(0.009)	(0.004)
External ownership	0.000	0.003	-0.000	0.003	0.000	0.003
	(0.004)	(0.003)	(0.004)	(0.003)	(0.004)	(0.003)
Board Characteristics						
Board size	0.079	-0.044	0.083	-0.047	0.081	-0.049
	(0.286)	(0.200)	(0.286)	(0.199)	(0.287)	(0.199)
Chairman family		-0.060		-0.059		-0.059
		(0.124)		(0.123)		(0.123)
Independent directors	-0.034	0.021	-0.021	0.020	-0.024	0.026
	(0.185)	(0.157)	(0.185)	(0.157)	(0.185)	(0.157)
Executive directors	-0.151	0.326	-0.153	0.330	-0.132	0.327
	(0.679)	(0.436)	(0.681)	(0.435)	(0.680)	(0.435)
Industry dummy variables	Yes	Yes	Yes	Yes	Yes	Yes
Year dummy variables	Yes	Yes	Yes	Yes	Yes	Yes
Country dummy variables	Yes	Yes	Yes	Yes	Yes	Yes
Number of observations	399	399	399	399	399	399
Number of groups	147	147	147	147	147	147

So far we used the absolute values of total executive compensation and its components. However, it is plausible to expect that relative value of these figures weighted with firm size may lead to healthier findings. Overall, the size of the compensation has a direct relationship with the size of the firms. We run our baseline models, using weighted values of compensation variables weighted with firm size measured by total assets and alternatively measured with sales. Firm sales were used as the variable was found to have a strong influence on executive compensation in many of the earlier studies (e.g. Kato and Long, 2005; Buck et al., 2008). In many instances the CEO compensation may have a direct correlation with the sales achieved by the firms in a given financial year and as such sales is most likely to have a large influence on executive pay and firm performance rather than the total assets as a measure.

We start with the ratio of total executive compensation to total assets and results are presented in Table 5.7, Models 1 and 2. In both models we find that the coefficient of total executive compensation to total assets is positive and statistically significant. This finding indicates that in the GCC companies an increase in the total compensation is likely to result in an increased firm performance. Our findings are in line with the results reported by Kato and Long (2005) on their study in the context of Chinese firms. Pan et al. (2009) reported a positive association between executive pay and firm performance in cases where the executives were offered equity-based compensation. However, since our study cannot take into account equity-based compensation (see footnote 23) the results cannot be compared with that of Pan et al. (2009). Our findings also differ from that of Kakani and Ray (2002) who reported an insignificant relationship between CEO pay and firm performance in the Indian firms.

The findings from Table 5.7 also confirm with the earlier studies conducted by Murphy (1985, 1999) and Fyre. These studies reported a positive association between executive compensation and firm performance. Similarly Specifically, Fyre (2004) used Tobin's Q as the measurement of firm performance to report a strong relationship between the two variables. Fyre (2004) has also found that executive compensation especially when it is equity based leads to higher Tobin's Q and consequently higher Tobin's Q leads to greater use of equity-based compensation to executives. The study has not found a positive and

statistically significant association between lagged measure of equity-based compensation and firm performance[23].

Table 5.6 Relative total executive compensation and Tobin's Q with firm size measured with total assets

This table presents coefficient estimates for fixed effects and random effects regressions estimating the relationship between corporate governance variables and performance using Tobin's Q as the dependent variable. Industry, year and country dummy variables control for the macroeconomic conditions. Robust standard errors are reported in parenthesis. ***, ** and * represents significance levels at 1%, 5% and 10%, respectively. Definitions for all the variables are provided in Table 5.1.

Independent Variable	Model 1		Model 2	
	Fixed Effects	Random Effects	Fixed Effects	Random Effects
Compensation Structure				
Total executive compensation to total assets	0.222*	0.126*	0.281**	0.184***
	(0.110)	(0.060)	(0.099)	(0.051)
Firm Characteristics				
Firm size	-0.112	-0.044		
	(0.156)	(0.056)		
Sales			0.099*	0.059
			(0.047)	(0.031)
Leverage	-1.497***	-1.403***	-1.525***	-1.498***
	(0.360)	(0.235)	(0.346)	(0.226)
Ownership Structure				
Concentrated ownership	0.021	-0.041	0.032	-0.045
	(0.081)	(0.049)	(0.079)	(0.049)
Managerial ownership	0.052*	0.008	0.053*	0.007
	(0.024)	(0.006)	(0.023)	(0.006)
Foreign ownership	0.181	0.098	0.163	0.063
	(0.244)	(0.138)	(0.239)	(0.139)
Family ownership	-0.061**	-0.011**	-0.063**	-0.011*
	(0.020)	(0.004)	(0.020)	(0.004)
Government ownership	0.008	0.002	0.005	0.002
	(0.013)	(0.005)	(0.012)	(0.005)
External ownership	0.001	0.005	0.001	0.004
	(0.003)	(0.002)	(0.003)	(0.002)
Board Characteristics				
Board size	0.258	0.015	0.239	-0.095
	(0.465)	(0.232)	(0.454)	(0.233)
Chairman family	-0.013	0.182	-0.009	0.142
	(0.478)	(0.118)	(0.468)	(0.121)
Independent directors	0.007	0.004	0.011	0.016
	(0.312)	(0.245)	(0.306)	(0.245)
Executive directors	-0.101	0.484	-0.099	0.400
	(0.886)	(0.507)	(0.867)	(0.510)
Industry dummy variables	Yes	Yes	Yes	Yes
Year dummy variables	Yes	Yes	Yes	Yes
Country dummy variables	Yes	Yes	Yes	Yes
Number of observations	1,014	1,014	1,005	1,005
Number of groups	295	295	295	295

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[23] The findings of this study are not comparable with Fyre (2004) since our study cannot take into account equity-based compensation due to this type of compensation being illegal in the GCC countries.

Thus, the general agency theory perspective as advocated by Jensen and Meckling (1976) does not appear to apply to the GCC context. As observed earlier, agency theory predicts that presence of diverging interests of the principal and agent the executives are likely to act in their own interest leaving the interest of the owners aside. However, the region-specific working conditions of executives prevailing in GCC region prevent the happening of any incidence that would contribute to agency conflicts in the region.

In Models 1 and 2 in Table 5.8, we use the ratio of compensation indicators to sales. We find that, surprisingly, ratio of total executive compensation to sales has a negative and significant coefficient. In other words, as the as the total executive compensation increases in respective to sales, GCC firms perform worse. This can be explained as follows. In the context of GCC firms, the absence of developed capital market does not facilitate arriving at the exact market value of equity which is a determining factor of the firm performance (Tobin's Q) for this study. Moreover the market value of equity of GCC firms is not largely affected by increase in the sales of such firms. Therefore, when the total executive compensation increases along with firm sales, no consequent positive impact could be observed in the Tobin's Q. This situation is possible when the owners consider any increase in the total assets of the firm only as tangible and better business performance and compensate the executives in appreciation of their contribution to increased total assets. Any increase in sales might be disregarded by them for compensating the executives. This might result in a negative relationship between executive pay in relation to sales and Tobin's Q.

In this context, Ghosh (2003) argues that irrespective of the size of the firm, performance of the firm increases with the increase in total executive compensation, however, at a decreasing rate in the context of Indian companies. Ghosh (2003) in effect points out that lower level of executive compensation, motivates the executives to work further towards improving the firm performance. As it applies to the GCC context, executives are motivated to perform better when they are offered differential salaries for varying executive levels, which in turn may lead to the conclusion that executive pay does not have strong association with firm performance as a whole. Therefore, from the findings of Ghosh (2003), it can be inferred that there is only a marginal relationship between executive pay and firm performance and this finding is similar to the findings of this study.

Table 5.7 Relative total executive compensation and Tobin's Q with firm size measured with sales

This table presents coefficient estimates for fixed effects and random effects regressions estimating the relationship between corporate governance variables and performance using Tobin's Q as the dependent variable. Industry, year and country dummy variables control for the macroeconomic conditions. Robust standard errors are reported in parenthesis. ***, ** and * represents significance levels at 1%, 5% and 10%, respectively. See Table 5.1 for exact definitions of variables.

Independent Variable	Model 1		Model 2	
	Fixed Effects	Random Effects	Fixed Effects	Random Effects
Compensation Structure				
Total executive compensation to sales	-0.005*	-0.005*	-0.005*	-0.005*
	(0.002)	(0.002)	(0.002)	(0.002)
Firm Characteristics				
Firm size	-0.256	-0.119*		
	(0.142)	(0.047)		
Sales			0.148*	0.034
			(0.063)	(0.035)
Leverage	-1.539***	-1.388***	-1.704***	-1.619***
	(0.357)	(0.238)	(0.346)	(0.230)
Ownership Structure				
Concentrated ownership	-0.002	-0.050	0.018	-0.056
	(0.081)	(0.050)	(0.080)	(0.050)
Managerial ownership	0.051*	0.008	0.052*	0.006
	(0.023)	(0.006)	(0.023)	(0.006)
Foreign ownership	0.185	0.088	0.142	0.033
	(0.241)	(0.140)	(0.240)	(0.140)
Family ownership	-0.060**	-0.012**	-0.065**	-0.012**
	(0.020)	(0.004)	(0.020)	(0.004)
Government ownership	0.006	0.003	0.004	0.001
	(0.013)	(0.005)	(0.013)	(0.005)
External ownership	0.002	0.006*	0.002	0.006*
	(0.004)	(0.003)	(0.004)	(0.003)
Board Characteristics				
Board size	0.285	0.058	0.254	-0.111
	(0.488)	(0.240)	(0.487)	(0.240)
Chairman family	-0.025	0.202	-0.018	0.181
	(0.470)	(0.121)	(0.470)	(0.122)
Independent directors	-0.005	0.004	0.032	0.040
	(0.313)	(0.248)	(0.313)	(0.250)
Executive directors	0.015	0.518	0.090	0.387
	(0.874)	(0.517)	(0.873)	(0.519)
Industry dummy variables	Yes	Yes	Yes	Yes
Year dummy variables	Yes	Yes	Yes	Yes
Country dummy variables	Yes	Yes	Yes	Yes
Number of observations	1,000	1,000	1,000	1,000
Number of groups	294	294	294	294

In Models 1 and 2 in Table 5.9, we employ the ratio of salary to total assets as the main indicator for executive compensation. However, we do not find any significant relationship between salary to total assets and Tobin's Q. In Model 1 and Model 2 in

Table 5.10, the ratio of salary to sales was employed to test its effect on firm performance. Again we do not detect a significant relationship.

We also utilise the ratio of bonuses paid to total firm size, measured either by total assets or sales. The results are presented in Table 5.11 in Models 1 and 2 and Models 3 and 4, respectively. Both fixed effect and random effect regression show that a significant relationship does not exist between bonuses paid and firm performance.

In Models 1 and 2 in Table 5.12, we looked at the limited sample where we know the breakdown of salary and bonus information. In Model 1 the ratio of total executive compensation with firm size was considered for its impact on the firm performance along with log of firm size. The regression analysis for both models has also shown an insignificant impact of the ratio of total executive compensation on firm performance. In Model 2, where the ratio of total executive compensation with firm size was considered with log of firm sales, the results of both fixed effects and random effects in this model do not show any statistically significant association between the variables. From the results presented in Table 5.11 and Table 5.12 on the regression where the ratio of the bonus and the ratio of the total executive compensation with the firm size and sales are used as independent variables, it is seen that the ratio of bonus to total executive compensation does not have any effect on firm performance.

Table 5.8 Relative salary and Tobin's Q with firm size measured with total assets

This table presents coefficient estimates for fixed effects and random effects regressions estimating the relationship between corporate governance variables and performance using Tobin's Q as the dependent variable. Industry, year and country dummy variables control for the macroeconomic conditions. Robust standard errors are reported in parenthesis. ***, ** and * represents significance levels at 1%, 5% and 10%, respectively. Definitions for all the variables are provided in Table 5.1.

Independent Variable	Model 1 Fixed Effects	Model 1 Random Effects	Model 2 Fixed Effects	Model 2 Random Effects
Compensation Structure				
Salary to total assets	0.076	-0.099	-0.000	-0.025
	(0.273)	(0.106)	(0.187)	(0.080)
Firm Characteristics				
Firm size	0.104	-0.061		
	(0.243)	(0.065)		
Sales			0.022	0.011
			(0.034)	(0.026)
Leverage	0.209	-0.437	0.264	-0.525*
	(0.382)	(0.243)	(0.370)	(0.226)
Ownership Structure				
Concentrated ownership	-0.059	-0.079	-0.062	-0.081
	(0.101)	(0.052)	(0.100)	(0.052)
Managerial ownership	0.014	0.005	0.016	0.004
	(0.021)	(0.005)	(0.021)	(0.005)
Foreign ownership	0.136	0.028	0.144	-0.001
	(0.148)	(0.114)	(0.147)	(0.111)
Family ownership	-0.013	-0.003	-0.014	-0.003
	(0.020)	(0.004)	(0.020)	(0.004)
Government ownership	0.006	0.004	0.006	0.003
	(0.009)	(0.004)	(0.009)	(0.004)
External ownership	0.000	0.003	0.000	0.003
	(0.004)	(0.003)	(0.004)	(0.003)
Board Characteristics				
Board size	0.070	-0.022	0.082	-0.056
	(0.287)	(0.203)	(0.287)	(0.202)
Chairman family		-0.053		-0.057
		(0.123)		(0.123)
Independent directors	-0.022	0.015	-0.024	0.023
	(0.185)	(0.156)	(0.185)	(0.157)
Executive directors	-0.130	0.317	-0.133	0.312
	(0.680)	(0.438)	(0.681)	(0.438)
Industry dummy variables	Yes	Yes	Yes	Yes
Year dummy variables	Yes	Yes	Yes	Yes
Country dummy variables	Yes	Yes	Yes	Yes
Number of observations	400	400	399	399
Number of groups	147	147	147	147

Table 5.9 Relative salary and Tobin's Q with firm size measured with sales

This table presents coefficient estimates for fixed effects and random effects regressions estimating the relationship between corporate governance variables and performance using Tobin's Q as the dependent variable. Industry, year and country dummy variables control for the macroeconomic conditions. Robust standard errors are reported in parenthesis. ***, ** and * represents significance levels at 1%, 5% and 10%, respectively. Definitions for all the variables are provided in Table 5.1.

Independent Variable	Model 1 Fixed Effects	Model 1 Random Effects	Model 2 Fixed Effects	Model 2 Random Effects
Compensation Structure				
Salary to sales	-0.004	-0.001	-0.002	0.001
	(0.009)	(0.008)	(0.009)	(0.009)
Firm Characteristics				
Firm size	0.040	-0.020		
	(0.169)	(0.048)		
Sales			0.031	0.023
			(0.068)	(0.037)
Leverage	0.219	-0.474	0.243	-0.553*
	(0.390)	(0.246)	(0.366)	(0.234)
Ownership Structure				
Concentrated ownership	-0.057	-0.079	-0.061	-0.082
	(0.102)	(0.052)	(0.098)	(0.052)
Managerial ownership	0.015	0.005	0.016	0.005
	(0.021)	(0.005)	(0.021)	(0.005)
Foreign ownership	0.148	0.025	0.146	-0.000
	(0.149)	(0.115)	(0.149)	(0.113)
Family ownership	-0.013	-0.004	-0.014	-0.003
	(0.020)	(0.004)	(0.020)	(0.004)
Government ownership	0.005	0.003	0.005	0.003
	(0.009)	(0.004)	(0.009)	(0.004)
External ownership	0.000	0.003	0.000	0.003
	(0.004)	(0.003)	(0.004)	(0.003)
Board Characteristics				
Board size	0.056	-0.035	0.062	-0.068
	(0.319)	(0.215)	(0.317)	(0.209)
Chairman family		-0.053		-0.060
		(0.123)		(0.123)
Independent directors	-0.034	0.003	-0.028	0.019
	(0.191)	(0.161)	(0.192)	(0.162)
Executive directors	-0.192	0.333	-0.167	0.318
	(0.697)	(0.447)	(0.699)	(0.444)
Industry dummy variables	Yes	Yes	Yes	Yes
Year dummy variables	Yes	Yes	Yes	Yes
Country dummy variables	Yes	Yes	Yes	Yes
Number of observations	394	394	394	394
Number of groups	146	146	146	146

Table 5.10 Relative bonus and Tobin's Q

This table presents coefficient estimates for fixed effects and random effects regressions estimating the relationship between corporate governance variables and performance using Tobin's Q as the dependent variable. Industry, year and country dummy variables control for the macroeconomic conditions. Robust standard errors are reported in parenthesis. ***, ** and * represents significance levels at 1%, 5% and 10%, respectively. See Table 5.1 for exact definitions of variables.

	Model 1 Fixed Effects	Model 1 Random Effects	Model 2 Fixed Effects	Model 2 Random Effects	Model 3 Fixed Effects	Model 3 Random Effects	Model 4 Fixed Effects	Model 4 Random Effects
Compensation Structure								
Bonus to total assets	-0.023	-0.012	-0.026	0.006				
	(0.079)	(0.065)	(0.077)	(0.058)				
Bonus to sales					-0.003	-0.000	-0.001	0.002
					(0.009)	(0.009)	(0.010)	(0.009)
Firm Characteristics								
Firm size	0.042	-0.025			0.043	-0.019		
	(0.171)	(0.054)			(0.168)	(0.048)		
Sales			0.022	0.013			0.033	0.024
			(0.034)	(0.025)			(0.068)	(0.037)
Leverage	0.222	-0.462	0.262	-0.511*	0.218	-0.475	0.242	-0.553*
	(0.383)	(0.242)	(0.361)	(0.225)	(0.390)	(0.246)	(0.366)	(0.234)
Ownership Structure								
Concentrated ownership	-0.052	-0.079	-0.054	-0.081	-0.056	-0.079	-0.061	-0.083
	(0.102)	(0.052)	(0.100)	(0.052)	(0.102)	(0.052)	(0.098)	(0.052)
Managerial ownership	0.014	0.005	0.015	0.005	0.014	0.005	0.016	0.005
	(0.021)	(0.005)	(0.021)	(0.005)	(0.021)	(0.005)	(0.021)	(0.005)
Foreign ownership	0.146	0.023	0.150	0.002	0.149	0.025	0.146	-0.001
	(0.149)	(0.114)	(0.148)	(0.111)	(0.149)	(0.115)	(0.149)	(0.113)
Family ownership	-0.012	-0.003	-0.013	-0.003	-0.013	-0.003	-0.014	-0.003
	(0.020)	(0.004)	(0.020)	(0.004)	(0.020)	(0.004)	(0.020)	(0.004)
Government ownership	0.006	0.004	0.006	0.003	0.005	0.003	0.005	0.003
	(0.009)	(0.004)	(0.009)	(0.004)	(0.009)	(0.004)	(0.009)	(0.004)
External ownership	0.000	0.003	-0.000	0.003	0.000	0.003	0.000	0.003
	(0.004)	(0.003)	(0.004)	(0.003)	(0.004)	(0.003)	(0.004)	(0.003)
Board Characteristics								
Board size	0.071	-0.015	0.080	-0.043	0.056	-0.035	0.062	-0.069
	(0.287)	(0.203)	(0.286)	(0.200)	(0.319)	(0.215)	(0.317)	(0.210)
Chairman family		-0.052		-0.059		-0.053		-0.061
		(0.123)		(0.123)		(0.123)		(0.123)
Independent directors	-0.019	0.012	-0.022	0.020	-0.034	0.003	-0.028	0.020
	(0.185)	(0.157)	(0.185)	(0.157)	(0.191)	(0.161)	(0.192)	(0.162)
Executive directors	-0.154	0.349	-0.151	0.332	-0.185	0.337	-0.157	0.320
	(0.681)	(0.437)	(0.682)	(0.436)	(0.698)	(0.447)	(0.700)	(0.444)
Industry dummy variables	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Year dummy variables	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Country dummy variables	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Number of observations	400	400	399	399	394	394	394	394
Number of groups	147	147	147	147	146	146	146	146

Some of the earlier empirical studies have considered stock options in the place of bonus and have found mixed evidence with respect to the relationship between pay and performance. For example, a strong and positive association between stock options in the executive compensation and firm performance has been reported by Fung et al. (2001) and Matsunaga and Park (2001). Murphy (1999) has reported a strong and positive association between stock options and firm performance. Absence stock options as a form of executive compensation in GCC has prevented the comparison of the findings of this study with those of earlier studies that focused on the pay performance relationship where granting stock options is a form of remunerating the executives.

Although there are some studies focusing on firm performance on the basis of ownership structure and corporate governance in the context of GCC countries, studies that examined the direct link between executive pay and firm performance are rather limited in number; thus providing meagre scope for comparison of the findings of this study with those of earlier studies with respect to GCC companies. One of the recent studies by Hassan and Halbouni (2013) report that differing results can be obtained by using Tobin's Q as the basis of measurement when accounting based firm performance is used rather than market based firm performance to analyse the impact of executive compensation on the firm performance. On the basis of their study on the relationship between corporate governance principles and firm performance, Aljifri and Moustafa (2007) report that linking pay to performance may not be a successful means of monitoring and motivating management, although their study did not focus on the testing of the relationship between executive compensation and firm performance. Therefore, this study infers that Aljifri and Moustafa (2007) did not support the view that executive pay has any effect on firm performance. Adopting this view, it can be stated that the findings of this study differ from those of Aljifri and Moustafa (2007) in the context of GCC countries. The recent study by Al-Matar et al. (2014) has also reported a weak and insignificant relationship between pay and performance in respect of Omani companies. However, the scope the study by Al-Matar et al. (2014) was different as they examined the impact of governance variables. Hence the findings of Al-Matar et al. (2014) might be different from those of this study. The findings of this study are in line with Hasan et al. (2014) who reported a positive and significant pay-performance relationship. Since the findings of the earlier studies pertaining to the

Table 5.11 Total executive compensation and Tobin's Q with limited sample

This table presents coefficient estimates for fixed effects and random effects regressions estimating the relationship between corporate governance variables and performance using Tobin's Q as the dependent variable. Industry, year and country dummy variables control for the macroeconomic conditions. Robust standard errors are reported in parenthesis. ***, ** and * represents significance levels at 1%, 5% and 10%, respectively. Definitions for all the variables are provided in Table 5.1.

	Model 1		Model 2	
	Fixed Effects	Random Effects	Fixed Effects	Random Effects
Compensation Structure				
Total executive compensation to total assets	0.124	-0.067	0.029	0.003
	(0.266)	(0.119)	(0.191)	(0.085)
Firm Characteristics				
Firm size	0.130	-0.049		
	(0.232)	(0.069)		
Sales			0.022	0.013
			(0.034)	(0.026)
Leverage	0.207	-0.449	0.276	-0.512*
	(0.382)	(0.243)	(0.370)	(0.228)
Ownership Structure				
Concentrated ownership	-0.061	-0.080	-0.066	-0.081
	(0.101)	(0.052)	(0.100)	(0.052)
Managerial ownership	0.014	0.005	0.016	0.005
	(0.021)	(0.005)	(0.021)	(0.005)
Foreign ownership	0.131	0.027	0.143	0.003
	(0.148)	(0.114)	(0.147)	(0.111)
Family ownership	-0.013	-0.003	-0.014	-0.003
	(0.020)	(0.004)	(0.020)	(0.004)
Government ownership	0.006	0.004	0.006	0.003
	(0.009)	(0.004)	(0.009)	(0.004)
External ownership	0.000	0.003	0.000	0.003
	(0.004)	(0.003)	(0.004)	(0.003)
Board Characteristics				
Board size	0.066	-0.021	0.084	-0.044
	(0.287)	(0.204)	(0.287)	(0.202)
Chairman family		-0.048		-0.058
		(0.123)		(0.123)
Independent directors	-0.022	0.013	-0.025	0.020
	(0.185)	(0.157)	(0.185)	(0.157)
Executive directors	-0.111	0.342	-0.123	0.331
	(0.681)	(0.437)	(0.682)	(0.437)
Industry dummy variables	Yes	Yes	Yes	Yes
Year dummy variables	Yes	Yes	Yes	Yes
Country dummy variables	Yes	Yes	Yes	Yes
Number of observations	400	400	399	399
Number of groups	147	147	147	147

relationship between executive compensation and firm performance in the context of GCC countries are inconclusive, the findings of this study are not exactly comparable with the findings of those earlier studies.

In order to extend the analysis to cover the impact of compensation structure on the Tobin's Q of the sample firms, we utilise lag variables for executive compensation. This is because there may be a link between previous year's compensation with current year's

performance. First we use lag of total executive compensation. The results of fixed and random effects regression results are presented in Table 5.13, Models 1 and 2. We do not find a statistically significant coefficient for the lagged total executive compensation and Tobin's Q.

Next we employ lag of total executive compensation to total assets. Results are represented in Models 3 and 4 of Table 5.13. Although three of the models show an insignificant coefficient, in Model 4 random effect regression we find a positive and a significant coefficient between lag of total executive compensation to total assets and firm performance. In Model 5 and 6 in Table 5.13, we report the results for the lag of total executive compensation to sales. However, we do not find a significant coefficient both in random and fixed effects.

As mentioned earlier, the relationship between executive compensation and firm performance in the context of GCC region has been studied mostly from the purview of governance issues including ownership structures rather than from the perspective of firm size or other firm-specific characteristics. Since the different economies in the GCC region have distinct institutional structure and culture the ownership structure has been found to be one of the dominant factors in influencing the managerial compensation rather than other firm-specific characteristics like sales or firm size. According to Al-Swidi et al. (2012) the infrastructure, culture and institutions are different in the GCC region and therefore the findings with respect pay-performance relationship cannot be compared with the findings of the studies conducted in the West and the United States. Therefore, in general this study argues that in the context of GCC region there cannot be a strong association between executive pay and firm performance when the firm-specific characteristics like firm size or sales are considered as control variables. The findings of this study can be compared with

Table 5.12 Compensation structure and Tobin's Q - with one year lagged compensation variables

This table presents coefficient estimates for fixed effects and random effects regressions estimating the relationship between corporate governance variables and performance using Tobin's Q as the dependent variable. Industry, year and country dummy variables control for the macroeconomic conditions. Robust standard errors are reported in parenthesis. ***, ** and * represents significance levels at 1%, 5% and 10%, respectively. Definitions for all the variables are provided in Table 5.1.

Independent Variable	Model 1		Model 2		Model 3		Model 4		Model 5		Model 6	
	Fixed Effects	Random Effects	Fixed Effects	Random Effects	Fixed Effects	Random Effects	Fixed Effects	Random Effects	Fixed Effects	Random Effects	Fixed Effects	Random Effects
Compensation Structure												
Total executive compensation (1 year lag)	0.054	0.016	0.032	-0.035								
	(0.052)	(0.040)	(0.052)	(0.040)								
Total executive compensation to total assets (1 year lag)					0.061	0.051	0.049	0.118*				
					(0.069)	(0.056)	(0.071)	(0.049)				
Total executive compensation to sales (1 year lag)									-0.001	-0.001	-0.001	-0.001
									(0.001)	(0.001)	(0.001)	(0.001)
Firm Characteristics												
Firm size	-0.351*	-0.129**			-0.332*	-0.102*			-0.359*	-0.127**		
	(0.149)	(0.047)			(0.146)	(0.051)			(0.150)	(0.044)		
Sales			0.096	0.044			0.081	0.043			0.162*	0.034
			(0.053)	(0.032)			(0.055)	(0.031)			(0.074)	(0.035)
Leverage	-1.501***	-1.285***	-1.706***	-1.525***	-1.516***	-1.293***	-1.715***	-1.484***	-1.584***	-1.329***	-1.840***	-1.611***
	(0.369)	(0.230)	(0.359)	(0.223)	(0.373)	(0.231)	(0.364)	(0.223)	(0.381)	(0.234)	(0.368)	(0.230)
Ownership Structure												
Concentrated ownership	0.022	-0.036	0.057	-0.046	0.023	-0.037	0.056	-0.045	0.027	-0.033	0.060	-0.041
	(0.083)	(0.048)	(0.082)	(0.049)	(0.083)	(0.048)	(0.082)	(0.049)	(0.084)	(0.048)	(0.083)	(0.049)
Managerial ownership	0.041	0.007	0.042	0.005	0.043	0.007	0.044	0.006	0.042	0.007	0.043	0.005
	(0.025)	(0.006)	(0.025)	(0.006)	(0.025)	(0.006)	(0.025)	(0.006)	(0.025)	(0.006)	(0.025)	(0.006)
Foreign ownership	0.182	0.096	0.151	0.042	0.198	0.100	0.161	0.047	0.208	0.099	0.151	0.030
	(0.282)	(0.138)	(0.281)	(0.141)	(0.282)	(0.138)	(0.281)	(0.140)	(0.284)	(0.138)	(0.283)	(0.142)
Family ownership	-0.056**	-0.011**	-0.062**	-0.011**	-0.056**	-0.011**	-0.062**	-0.011**	-0.054*	-0.011**	-0.059**	-0.011**
	(0.021)	(0.004)	(0.021)	(0.004)	(0.021)	(0.004)	(0.021)	(0.004)	(0.022)	(0.004)	(0.021)	(0.004)
Government ownership	0.006	0.002	0.003	0.000	0.006	0.002	0.003	0.001	0.007	0.002	0.004	-0.000
	(0.014)	(0.005)	(0.014)	(0.005)	(0.014)	(0.005)	(0.014)	(0.005)	(0.014)	(0.005)	(0.014)	(0.005)
External ownership	0.002	0.006*	0.002	0.006*	0.002	0.006*	0.002	0.006*	0.001	0.005*	0.001	0.005*
	(0.004)	(0.002)	(0.003)	(0.002)	(0.004)	(0.002)	(0.004)	(0.002)	(0.004)	(0.002)	(0.004)	(0.002)
Board Characteristics												
Board size	0.201	0.078	0.157	-0.082	0.193	0.085	0.151	-0.060	0.188	0.097	0.156	-0.095
	(0.497)	(0.228)	(0.495)	(0.232)	(0.498)	(0.228)	(0.496)	(0.231)	(0.509)	(0.229)	(0.506)	(0.234)
Chairman family	-0.063	0.240*	-0.047	0.205	-0.085	0.233*	-0.061	0.192	0.041	0.254*	0.114	0.219
	(0.471)	(0.113)	(0.469)	(0.116)	(0.471)	(0.114)	(0.470)	(0.116)	(0.493)	(0.114)	(0.490)	(0.118)
Independent directors	-0.014	0.016	-0.008	0.047	-0.025	0.020	-0.013	0.053	-0.025	0.028	0.016	0.063
	(0.323)	(0.247)	(0.322)	(0.249)	(0.323)	(0.247)	(0.322)	(0.248)	(0.326)	(0.249)	(0.325)	(0.252)
Executive directors	0.291	0.601	0.348	0.447	0.244	0.602	0.310	0.503	0.264	0.615	0.374	0.473
	(0.901)	(0.498)	(0.898)	(0.504)	(0.903)	(0.497)	(0.900)	(0.503)	(0.916)	(0.502)	(0.911)	(0.512)
Industry dummy variables	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Year dummy variables	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Country dummy variables	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Number of observations	970	970	961	961	964	964	955	955	949	949	941	941
Number of groups	295	295	295	295	295	295	295	295	294	294	292	292

those of Al-Matar et al. (2014) who have reported a positive but insignificant relationship between compensation and firm performance.

Overall, although this research establishes a relationship between total executive compensation and Tobin's Q in the case of GCC companies, the strength of the relationship is weak. Therefore, the findings of this study about the relationship between executive compensation and the performance of such firms point towards mixed results. The results of this study are comparable to some of the earlier studies and they also contradict the findings of other earlier studies. In the context of the GCC firms this study has observed a weak association between pay and performance and this situation may arise because of many factors specific to the GCC employment environment and the ownership structure of the companies. First, a majority of the companies are owned by large families with sizeable controlling interests. Therefore, the governance issues peculiar to the GCC companies do not give rise to any agency conflicts leading to the adoption of motivation policies through remunerating the executives for ensuring better performance of the firms. Secondly, a large number of executives are expatriate population. The expatriate executives may not have any real interest in ensuring the long-term sustainability and growth of the companies as there is no sense of belonging or permanency of relationship between them and the employer firms beyond the contract periods. As discussed earlier, therefore, the executive pay and performance in the GCC context may be approached from a tournament theoretical perspective where the executive remuneration can be related to individual performance rather than the firm performance. These factors specific to the GCC region drive to the point there can be no direct link between executive pay and firm performance in respect of GCC companies.

5.4.3 Robustness Check

5.4.3.1 Lagged variables

We repeat our results of the estimations for the fixed effects regressions models with lagged values for independent firm characteristics variables to check the robustness of our findings

in respect of compensation structure and Tobin's Q. First, in Table 5.14 (Appendix A) we re-estimate the regressions models with lagged values for firm characteristics variables. The results strongly support the previous findings; however, the variations in the relationship coefficients show statistically significant deviations in the same line as that of the original fixed effects regression. We observe more pronounced negativity in the case of both firm size and leverage where one year lag values are used to test the robustness. In the case of other variables we observe modest variations in the coefficient values showing insignificant changes in the relationship because of the inclusion of lag values.

Second, we re-estimate the fixed effect regressions models with lagged values for firm characteristics variables for checking the robustness of original findings in respect of relative total executive compensation and Tobin's Q with firm size measured with total assets and sales. The results in Table 5.15 (Appendix A) represent the findings from the robustness tests. From the findings we find that there are no significant variations in the relationship between total executive compensation to total assets and total executive compensation to sales because of the inclusion of the lagged values in some of the firm characteristics. In respect of other variables, we have observed statistically insignificant variations in the coefficient values indicating minor variations because of the use of lagged values. Thus the robustness check supports the findings of the original fixed effects regression.

5.4.3.2 Interactions Variables

We repeat our results of the estimations for the fixed effects regressions models with interact various ownership variables. We interacts total executive compensation to total assets with managerial ownership and total executive compensation to total assets with family ownership to test whether the new interacted variables makes a difference. Also, we interacts total executive compensation to sales with managerial ownership and total executive compensation to sales with family ownership. The results of the robustness check included in Table 5.16 (Appendix A) support the original findings. From the findings of the robustness check we have not observed any statistically significant variations in the regression results of Model 3 and Model 4 which included interaction variables. We have found some variation

in respect of the variable managerial ownership in the robustness regression conducted. However, the variation observed has not been significant.

The results of the robustness test where the interaction variables were included are reported in Table 5.17 (Appendix A). We find that the results of the robustness check completely support the findings of the original fixed effects regression results as we have not found any significant deviations in the robustness check. In respect of all the variables in both Model 1 and Model 2, we have not observed significant variations in the relationship coefficient values.

5.5 Conclusion

This paper examines the relationship between executive compensation and firm performance, measured by Tobin's Q, in 295 listed non-financial companies operating in Gulf economies of Kuwait, Oman, Qatar, Saudi Arabia, and United Arab Emirates for the period of 2006-2011. The empirical findings reveal that there is a positive and statistically significant relationship between the ratio of total executive compensation to total assets and firm performance. In selected models we find that total executive compensation to sales provided results showing a negative and significant relationship between pay and performance. While any increase in the size of executive compensation in relation to total assets might increase the Tobin's Q, same result cannot be expected in the Tobin's with an increase in executive pay in relation to sales. This may be because the owners might consider the increase in the assets value as more tangible business performance than an increase in the sales and accordingly they might decide to compensate the executives more whenever they observe an increase in the total assets of the company. On the other hand, we do not find any statistically significant relationship between Tobin's Q and the components of compensation, namely salary and bonus. We interpret the findings of this study to point out that specific GCC economic environment and features peculiar to this region has more impact on the firm performance rather than the executive compensation. Nevertheless, in one of the random effect regression models, we find a positive and a significant coefficient between lagged of total executive compensation to total assets and firm performance. Therefore, it is argued that when the compensation figures are scald with firm size represented by total assets, the empirical results would become meaningful to assess the relationship between executive pay and performance in the GCC firms.

The robustness check performed in respect of compensation structure and Tobin's Q showed more pronounced negativity in the case of both firm size and leverage where one year lag values are used to test the robustness. The findings of robustness check indicated that there are no significant variations in the relationship between total executive compensation to total assets and total executive compensation to sales because of the inclusion of the lagged values in some of the firm characteristics. In respect of other variables, statistically insignificant

variations in the coefficient values were observed in the robustness check. The robustness check with interaction variables in the case of relative total executive compensation and Tobin's Q with firm size measured with total assets has not indicated any statistically significant deviations; thus supporting the original regression findings. Similarly, the robustness check has not revealed any significant deviations from the original findings in respect of relative total executive compensation and Tobin's Q with firm size measured with sales.

This study concludes that the distinct institutional structure and culture specific to the GCC economies might be one of the dominant factors that influence the managerial compensation in the different economies and as such firm-specific characteristics such as firm size or sales are not likely to affect the executive compensation levels. Therefore, the findings of this study may not be comparable to the findings of similar studies conducted in the research settings of other advanced economies. This study argues that perhaps the distinct ownership structure and prevalence of large expatriate executives might affect the pay-performance relationship in the GCC context. This study also argues that the relationship between executive pay and performance in the GCC context may be approached from a tournament theoretical perspective where individual executive performance may be the determinant for the level of compensation payable with no relevance to firm performance. These arguments point to the premise that generally there can be no direct link between executive compensation and firm performance in the GCC countries when the firm performance is subject to the influence of control variables of firm-specific characteristics like firm size or firm sales.

This study is the first of its type in the context of GCC countries and since most of the results are not consistent with the findings of previous studies, further examination of the pay-performance relationship may be necessary. There are many factors such as the unavailability of segregated total compensation into its different components which led to limitations on availability of comprehensive data which may have biased the findings of this study. Comparability of the findings of this study with earlier studies that focused on stock options is also limited because of the non-existence of the practice of offering stock options to executives in GCC countries. Limited prior research on the topic in GCC countries is another limitation that affected the theoretical richness of this study.

The findings of the study open up further areas of research in any specific industry or smaller number of samples is likely to throw further light on the relationship between pay and performance in the case of executives working in the listed companies in GCC countries by undertaking a qualitative research in the intensity of different factors affecting the determinations of executive compensation within that specific industry. Comparative studies of the relationship between pay and performance with other emerging economies may also provide information on the specificities of the Gulf economies to affect such relationship.

Appendix A

Table 5.13 Compensation structure and Tobin's Q- the baseline model-Lagged Firm Characteristics

This table presents coefficient estimates for fixed effects regressions estimating the relationship between corporate governance variables and performance using Tobin's Q as the dependent variable. Industry, year and country dummy variables control for the macroeconomic conditions. Robust standard errors are reported in parenthesis. ***, ** and * represents significance levels at 1%, 5% and 10%, respectively. See Table 5.1 for exact definitions of variables.

Independent Variable	Model 1	Model 2	Model 3	Model 4
Compensation Structure				
Total executive compensation	0.021			
	(0.054)			
Salary		0.050		
		(0.067)		
Bonuses			-0.006	
			(0.016)	
Bonus to total compensation				-0.008
				(0.218)
Firm Characteristics				
Firm size (1 year lag)	-0.079	0.141	0.171	0.168
	(0.101)	(0.155)	(0.151)	(0.152)
Leverage (1 year lag)	-1.000**	0.030	0.018	0.025
	(0.351)	(0.333)	(0.333)	(0.333)
Ownership Structure				
Concentrated ownership	0.040	-0.059	-0.060	-0.064
	(0.084)	(0.096)	(0.097)	(0.096)
Managerial ownership	0.056*	0.015	0.016	0.017
	(0.024)	(0.021)	(0.021)	(0.021)
Foreign ownership	0.203	0.122	0.137	0.129
	(0.252)	(0.147)	(0.148)	(0.147)
Family ownership	-0.065**	-0.013	-0.014	-0.014
	(0.021)	(0.020)	(0.020)	(0.020)
Government ownership	0.002	0.006	0.007	0.006
	(0.013)	(0.009)	(0.009)	(0.009)
External ownership	0.002	0.001	0.000	0.001
	(0.004)	(0.004)	(0.004)	(0.004)
Board Characteristics				
Board size	0.364	0.018	0.011	0.011
	(0.474)	(0.289)	(0.289)	(0.290)
Chairman family	-0.041			
	(0.511)			
Independent directors	-0.069	-0.030	-0.018	-0.022
	(0.319)	(0.184)	(0.184)	(0.184)
Executive directors	-0.035	-0.103	-0.098	-0.081
	(0.901)	(0.679)	(0.681)	(0.680)
Industry dummy variables	Yes	Yes	Yes	Yes
Year dummy variables	Yes	Yes	Yes	Yes
Country dummy variables	Yes	Yes	Yes	Yes
Number of observations	998	395	395	395
Number of groups	294	145	145	145

Table 5.14 Relative total executive compensation and Tobin's Q with firm size measured with total assets and sales-Lagged Firm Characteristics

This table presents coefficient estimates for fixed effects regressions estimating the relationship between corporate governance variables and performance using Tobin's Q as the dependent variable. Industry, year and country dummy variables control for the macroeconomic conditions. Robust standard errors are reported in parenthesis. ***, ** and * represents significance levels at 1%, 5% and 10%, respectively. Definitions for all the variables are provided in Table 5.1.

Independent Variable	Model 1	Model 2	Model 3	Model 4
Compensation Structure				
Total executive compensation to total assets	0.280**	0.278**		
	(0.102)	(0.102)		
Total executive compensation to sales			-0.005*	-0.006*
			(0.002)	(0.002)
Firm Characteristics				
Firm size (1 year lag)	-0.043		-0.090	
	(0.101)		(0.101)	
Sales (1 year lag)		0.070		0.066
		(0.041)		(0.043)
Leverage (1 year lag)	-0.996**	-1.008**	-1.064**	-1.086**
	(0.349)	(0.349)	(0.349)	(0.349)
Ownership Structure				
Concentrated ownership	0.026	0.026	0.017	0.021
	(0.084)	(0.084)	(0.083)	(0.084)
Managerial ownership	0.055*	0.055*	0.054*	0.055*
	(0.024)	(0.024)	(0.024)	(0.024)
Foreign ownership	0.203	0.202	0.205	0.197
	(0.250)	(0.251)	(0.247)	(0.247)
Family ownership	-0.063**	-0.062**	-0.064**	-0.063**
	(0.021)	(0.021)	(0.020)	(0.020)
Government ownership	0.004	0.004	0.001	0.001
	(0.013)	(0.013)	(0.013)	(0.013)
External ownership	0.002	0.001	0.004	0.003
	(0.004)	(0.004)	(0.004)	(0.004)
Board Characteristics				
Board size	0.313	0.283	0.286	0.259
	(0.472)	(0.471)	(0.496)	(0.495)
Chairman family	-0.034	-0.032	-0.040	-0.029
	(0.508)	(0.508)	(0.501)	(0.500)
Independent directors	-0.059	-0.070	-0.098	-0.101
	(0.317)	(0.317)	(0.318)	(0.318)
Executive directors	-0.211	-0.216	-0.098	-0.087
	(0.899)	(0.900)	(0.890)	(0.890)
Industry dummy variables	Yes	Yes	Yes	Yes
Year dummy variables	Yes	Yes	Yes	Yes
Country dummy variables	Yes	Yes	Yes	Yes
Number of observations	998	990	985	978
Number of groups	294	293	293	292

Table 5.15 Relative total executive compensation and Tobin's Q with firm size measured with total assets-Interaction variables

This table presents coefficient estimates for fixed effects and random effects regressions estimating the relationship between corporate governance variables and performance using Tobin's Q as the dependent variable. Industry, year and country dummy variables control for the macroeconomic conditions. Robust standard errors are reported in parenthesis. ***, ** and * represents significance levels at 1%, 5% and 10%, respectively. Definitions for all the variables are provided in Table 5.1.

Independent Variable	Model 1	Model 2	Model 3	Model 4
Compensation Structure				
Total executive compensation to total assets	0.222*	0.281**	0.199	0.211*
	(0.110)	(0.099)	(0.111)	(0.101)
Firm Characteristics				
Firm size	-0.112		-0.096	
	(0.156)		(0.156)	
Sales		0.099*		0.102*
		(0.047)		(0.047)
Leverage	-1.497***	-1.525***	-1.570***	-1.626***
	(0.360)	(0.346)	(0.363)	(0.346)
Ownership Structure				
Concentrated ownership	0.021	0.032	0.020	0.014
	(0.081)	(0.079)	(0.081)	(0.079)
Managerial ownership	0.052*	0.053*	0.001	0.061**
	(0.024)	(0.023)	(0.043)	(0.023)
Foreign ownership	0.181	0.163	0.176	0.157
	(0.244)	(0.239)	(0.244)	(0.237)
Family ownership	-0.061**	-0.063**	-0.063**	-0.134***
	(0.020)	(0.020)	(0.020)	(0.031)
Government ownership	0.008	0.005	0.008	0.006
	(0.013)	(0.012)	(0.013)	(0.012)
External ownership	0.001	0.001	0.001	0.001
	(0.003)	(0.003)	(0.003)	(0.003)
Total executive compensation to total assets*Managerial ownership			0.023	
			(0.016)	
Total executive compensation to total assets*Family ownership				0.026**
				(0.009)
Board Characteristics				
Board size	0.258	0.239	0.293	0.195
	(0.465)	(0.454)	(0.465)	(0.452)
Chairman family	-0.013	-0.009	-0.014	-0.011
	(0.478)	(0.468)	(0.478)	(0.465)
Independent directors	0.007	0.011	-0.015	-0.032
	(0.312)	(0.306)	(0.313)	(0.305)
Executive directors	-0.101	-0.099	-0.089	-0.121
	(0.886)	(0.867)	(0.885)	(0.862)
Industry dummy variables	Yes	Yes	Yes	Yes
Year dummy variables	Yes	Yes	Yes	Yes
Country dummy variables	Yes	Yes	Yes	Yes
Number of observations	1,014	1,005	1,014	1,005
Number of groups	295	295	295	295

Table 5.16 Relative total executive compensation and Tobin's Q with firm size measured with sales-Interaction variables

This table presents coefficient estimates for fixed effects and random effects regressions estimating the relationship between corporate governance variables and performance using Tobin's Q as the dependent variable. Industry, year and country dummy variables control for the macroeconomic conditions. Robust standard errors are reported in parenthesis. ***, ** and * represents significance levels at 1%, 5% and 10%, respectively. See Table 5.1 for exact definitions of variables.

Independent Variable	Model 1	Model 2	Model 3	Model 4
Compensation Structure				
Total executive compensation to sales	-0.005*	-0.005*	-0.005*	-0.002
	(0.002)	(0.002)	(0.002)	(0.002)
Firm Characteristics				
Firm size	-0.256		-0.258	
	(0.142)		(0.142)	
Sales		0.148*		0.113
		(0.063)		(0.062)
Leverage	-1.539***	-1.704***	-1.527***	-1.545***
	(0.357)	(0.346)	(0.357)	(0.339)
Ownership Structure				
Concentrated ownership	-0.002	0.018	-0.007	0.051
	(0.081)	(0.080)	(0.081)	(0.078)
Managerial ownership	0.051*	0.052*	0.059*	0.023
	(0.023)	(0.023)	(0.024)	(0.023)
Foreign ownership	0.185	0.142	0.183	0.156
	(0.241)	(0.240)	(0.241)	(0.235)
Family ownership	-0.060**	-0.065**	-0.060**	-0.024
	(0.020)	(0.020)	(0.020)	(0.021)
Government ownership	0.006	0.004	0.007	0.003
	(0.013)	(0.013)	(0.013)	(0.012)
External ownership	0.002	0.002	0.002	0.001
	(0.004)	(0.004)	(0.004)	(0.003)
Total executive compensation to sales*Managerial ownership			-0.004	
			(0.003)	
Total executive compensation to sales*Family ownership				-0.001***
				(0.000)
Board Characteristics				
Board size	0.285	0.254	0.266	0.289
	(0.488)	(0.487)	(0.488)	(0.477)
Chairman family	-0.025	-0.018	-0.027	-0.013
	(0.470)	(0.470)	(0.470)	(0.460)
Independent directors	-0.005	0.032	0.015	0.017
	(0.313)	(0.313)	(0.313)	(0.306)
Executive directors	0.015	0.090	0.073	0.219
	(0.874)	(0.873)	(0.875)	(0.855)
Industry dummy variables	Yes	Yes	Yes	Yes
Year dummy variables	Yes	Yes	Yes	Yes
Country dummy variables	Yes	Yes	Yes	Yes
Number of observations	1,000	1,000	1,000	1,000
Number of groups	294	294	294	294

Chapter 6. Conclusions

This research is motivated by the increasing importance of GCC economies within the world economy and the lack of research on how corporate governance mechanisms work in these countries. We contribute to the existing research by providing empirical evidence on how corporate performance is affected by ownership structure and executive compensation in the GCC country companies. We test these relationships using a uniquely constructed and hand collected data of 349 listed companies in Kuwait, Saudi Arabia, Oman, Qatar and United Arab Emirates for the years between 2006 and 2011. We contribute to the existing literature in several ways. To our knowledge, this is the first study to examine the impact of different types of ownership structures on firm performance in the GCC countries as a whole. It is also the first to investigate the determinants of executive compensation in the GCC countries and how firms in the GCC remunerate their managers. Additionally, the impact of executive compensation on firm performance is rarely studied in the context of GCC countries. Our final contribution to the literature is related to the size and the coverage of the data that are mostly collected manually from annual reports of the companies.

In Chapter 2, through reviewing the previous literature on theories governing corporate governance, we formulated a theoretical base for the study through a discussion on how major theories of corporate governance evolved over time. In this chapter, we also reviewed the different approaches to corporate governance and presented an overview of corporate governance on emerging markets. The historical perspective of corporate governance in Gulf Countries is also overviewed in this chapter. We also discussed the state of empirical research in corporate governance in general as well as in the context of the GCC region. On the basis of the review of the related literature we find that the corporate governance practices and standards prevailing in the GCC countries are not comparable to those followed in the Western and other developed countries because of many challenges identified by previous research. Nevertheless, we find that there is a large scope for the implementation of globally comparable corporate governance practices in the GCC countries.

We examined the impact that ownership structure has on firm performance in Chapter 3. As postulated by Jensen and Meckling, (1976) the corporate governance practices of a firm are

largely influenced by the relationship between ownership structure and firm performance. In line with earlier studies, we investigated this relationship empirically for the GCC countries. We find that when insider owner happens to be the chairman of the firm, higher insider ownership results in better firm performance. Similarly, firms could ensure a better performance when there is large institutional ownership. Our study also finds that firms having large family ownership tend to show a worse financial performance in GCC. One of the findings of our study indicates that, when ROA is used as the performance measure, government ownership of firms has a negative association with performance.

Empirical examination of the key determinants of the executive compensation was covered in Chapter 4. We have made a distinction between bonus and salaries paid to top five executives while controlling for other determinants of executive compensation. In addition, we examined the choice of compensation methods (salary or bonus) used by the GCC firms in establishing a compensation structure. More specifically, we focused on how the firm characteristics, ownership structures and other corporate governance measures shape the structure of total executive compensation and orient the components of executive compensation such as behaviour (salary) and outcome (bonus). Our research also covered the factors that determine the choice of compensation type by the GCC firms. In Chapter 4, we find that, within the context of GCC, executives receive higher total compensation from firms that are comparatively larger or firms that have potential future growth. We also report that executives of firms having concentrated ownership structure tend to receive lower compensation while the executives of large family ownership are offered higher levels of compensation. Our study also provides evidence that higher total compensation is being paid to executives by companies having external ownership. The findings indicate that executives employed by larger firms and firms having higher extent of leverage receive larger behaviour-oriented compensation (i.e. salary). On the other hand, lower salaries are paid to executives engaged by firms having a chairman from the family and also by firms where there is a large presence of executive members in the board. We also report that executives are paid higher remuneration when there is higher managerial or institutional ownership. Firms having higher growth potential tend to pay higher outcome-oriented compensation. Bonus payments are also higher when the chairman is from the owning family and when there more executive members in the board. Firms that have ownership by managers and by

family opt to pay higher levels of outcome-oriented compensation. Overall, factors like firm size, the presence of executive members on the board, and managerial ownership are found to influence the choice between behaviour versus outcome oriented compensation largely.

In Chapter 5, we examined the relationship between executive compensation and firm performance in the GCC countries. We report only a weak evidence for a higher total executive compensation to result in better firm performance. We do not find any significant relationship between the components of compensation (salary and bonus) and firm performance in GCC region. Therefore, we conclude that specific GCC economic environment and features peculiar to this region has more impact on the firm performance rather than the executive compensation.

Findings of our study is valuable in assisting key decision-makers, such as the shareholders or policy makers, in enhancing firm performance through diversifying their ownership structures and utilising the right policies in compensation of executives in GCC countries. The research question on the factors that motivates particular types of ownership structure that will be followed and the potential impact of such ownership structure on firm performance in the GCC countries provide additional knowledge on the benefits in terms of firm performance of using a particular ownership structure. It may also help owners of family-owned enterprises providing them a comprehensive understanding of better corporate governance standards makes this study important.

Given that the GCC economies are keen in diversifying the economic development across varied sectors moving away from the oil sector, measuring the corporate governance for GCC firms will help in evaluating the success of the firms in their diversification efforts. Since executive compensation is one of the major components of the firms' incentive structure and occupies a central role in corporate governance our findings on executive compensation will help in assessing the quality of corporate governance in GCC firms and in turn the success of the firms in their diversification efforts. Since both economic theory and empirical evidence point out to the fact that a close association between executive compensation and firm performance is a pre-requisite for instituting an efficient compensation system, this study attempted to determine the existence and magnitude of such link in the GCC firms.

Existence of a weakened pay-performance relationship for top executives may possibly make GCC firms less effective in solving the agency problem. Such effect may exist because of the ownership structures of GCC firms. Therefore, the findings of this study have important implications for the listed firms in GCC countries. Listed companies in the region may take all efforts to align the interests of top executives and shareholders to some extent. Such an interest alignment may become stronger when the companies try to broad-base their shareholdings or take other measures to improve the interest alignment based on the findings of this study.

An alternative way to tackle agency problem is to align the interests of managers with that of the shareholders by linking their employment with their performance. Full understanding of the impact of executive compensation on firm performance in GCC countries will help the companies to take suitable decisions in the direction of linking firm performance with executive employment as well as with their compensation structures. The findings of this study are most likely to help listed companies of GCC firms in this area. The findings will provide insights in to the changes that are required to be brought in by GCC firms in the structure of executive compensation. Since the study covers a large sample across GCC countries, the findings of our study can be generalised and applied in the context of any GCC country. In addition, our study can be considered distinct and more exploratory than the earlier studies (e.g. Aljifri and Moustafa, 2007: Hassan and Halbouni, 2013; and Al-Swidi et al. 2012). As explained earlier, the empirical analyses conducted as a part of the study is expected to provide new, different and better understanding of the ground reality from different perspectives as compared to earlier research studies in the various aspects of corporate governance, ownership structure and executive compensation handled by this study with respect to GCC region.

It has been widely pointed out that poor corporate governance practices in GCC countries have seriously affected the firm performance in the region. It may be necessary for the policymakers to introduce tough regulations for promoting good corporate governance practices in these countries to ensure better firm performance. By requiring the suppliers and private sector companies to adopt good corporate governance practices, the regulators can accelerate the reformation of corporate sector. The findings of this study will be particularly

helpful to the policy-makers in identifying the weak corporate governance areas in GCC companies and introduce the necessary measures to strengthen those areas. Conformity of the corporate governance norms within GCC with international practices is an area that needs focus in the context of strengthening the corporate governance in GCC region. This research through its examination and reporting of existing corporate governance practices in the GCC can help the regulators to achieve higher integration of corporate governance practices of GCC with Western practices subject to the constraints specific to GCC region as identified by this study.

The thesis has certain limitations that need to be taken into consideration when interpreting the findings. In chapter 3, the study has certain limitations that would render the findings to apply subject to the consideration of such limitations. From the published accounts of the sample firms, it was possible to gather information only on the number of foreign shareholders. The information does not reveal the percentage of foreign shareholdings as it is not mandatory to provide this information in the published accounts. The data contained ownership details in respect of shareholdings in excess of 5% of the total shareholdings of any firm under study as the firms in GCC countries report on the shareholdings that are either greater than or equal to 5%. Lack of details about smaller shareholdings might vitiate the findings to some extent. In addition, some of the firms in GCC countries do not have the practice of reporting all information relating to their shareholding patterns. Therefore, the fact that some of the ownership details with respect to certain firms in some years might be missing is to be recognised. The study is limited only to GCC countries. This means that the results cannot be generalised to other countries taking into account structural differences in the economies of other countries from those of GCC countries.

The research in Chapter 4 might have suffered from some limitations affecting the findings to a certain extent. One of the major methodological limitations of this research pertains to the data collected for analysis. The limitation arose because of the reporting practices of companies operating within the GCC region. For example, it is not the practice of all companies in the GCC countries to report complete data pertaining to the top five executives. While some companies present a composite figure of total executive compensation without any break-down of details, other companies follow the practice of reporting the salaries and

bonus separately. There are also companies that report only salaries without any mention of other payments made to the executives. Lack of extensive research on the executive compensation in Gulf countries presented a limitation in building up a sound theoretical background to the research.

The analysis in Chapter 5 is the first of its type in the context of GCC countries and since most of the results are not consistent with the findings of previous studies, further examination of the pay-performance relationship may be necessary. There are many factors such as the unavailability of segregated total compensation into its different components which led to limitations on availability of comprehensive data which may have biased the findings of this study. Comparability of the findings of this study with earlier studies that focused on stock options is also limited because of the non-existence of the practice of offering stock options to executives in GCC countries. Limited prior research on the topic in GCC countries is another limitation that affected the theoretical richness of this study.

However, further research is needed to confirm the results of the present study by employing a longer sample period, different techniques and other variables. There are other issues that deserve further attention in future studies. First, further research can be conducted to examine the changes in the ownership structures because of changes in the market conditions and changes in government policies and consequent impact on the performance of companies. Second, a comparative study of the impact of ownership structure on firm performance in one of the GCC countries with that of another developing country will prove to be beneficial from the extension of knowledge point of view. Third, further research is needed with focus on additional measures that are not dealt with by this research. Such further research may involve finding additional constructs and study their impact on the levels and structures on executive compensation in the Gulf region. For instance, further research may examine role duality and CEO control over boards of GCC firms and presence of independent directors to assess the extent of their impact in the determination of executive compensation.

Fourth, corporate governance is another area that offers scope for further extensive research for its impact in deciding compensation structures in the GCC firms. Since the changes in the economic and political environments are likely to bring about many changes in corporate governance mechanisms of GCC countries, a comparative study of the latest changes in

corporate governance measures in GCC countries with those being followed in developed countries in so far as they affect the executive compensation levels is likely to provide extended knowledge on the determination of executive compensation by companies in the GCC region. For example, the effect of formation of remuneration committees in the board and its impact on the determination of compensation in GCC countries as compared to Western countries is a probable area of further research.

Fifth, the findings of the study open up further areas of research in any specific industry or smaller number of samples is likely to throw further light on the relationship between pay and performance in the case of executives working in the listed companies in GCC countries by undertaking a qualitative research in the intensity of different factors affecting the determinations of executive compensation within that specific industry.

Finally, comparative studies of the relationship between pay and performance with other emerging economies may also provide information on the specificities of the Gulf economies to affect such relationship.

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