
Empirical Investigation into the impact of Corporate Governance on Stock Returns in Pakistan: Evidence from Financial Sector of Pakistan

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ABSTRACT

This study aims to investigate the impact of corporate governance on stock returns of commercial banks in Pakistan. Secondary data obtained and used from annual reports of banks and the Pakistan Stock Exchange database over a period from 2016-2020. The regression model is used to determine the influence of corporate governance on the stock returns in the banking sector. The results suggest that board size, a block of common shares, and individual & family block holdings have a significantly positive influence on stock returns while the board fraction, insiders' block holdings, industrial block holdings, and firm leverage are negatively associated with stock returns. The findings provided practical implications for the firms striving to enhance better corporate governance mechanism to avail maximum stock returns.

Key Words: Corporate Governance, Stock Returns, Pakistan Stock Exchange, Commercial Banks, Block holdings

1. INTRODUCTION

Corporate governance is a mechanism in which the resources of a firm are justifiably utilized and helps the organization in accomplishing its corporate goals. Corporate governance generates future opportunities for businesses by strengthening their governance structure (Rostami, Kohansal, 2016). Governance includes a wide range of practices that varies from laws relating to financial disclosure, to the structure of the board of the corporation and from the style and rules of the management to shareholder's rights. Corporate governance defines the management, the real owners (shareholders) of the firm and also the rules under which the affairs of the firm are regulated, and a set of practices under which the two entities collaborate and interact with each other (shareholder and management). Corporate governance has great implications on the organization's employment system, capital market, etc., therefore, improvement in corporate governance will result in changes in the structure and conduct of the business of a particular country (Marouan, Kouki. And Moez, 2015).

According to Pacy & Sifuna (2012) in the aftermath of the collapse of prominent U.S firms in 2002, an Act called Sarbanes-Oxley was passed that concentrated its emphasis on the role of corporate

governance in the eradication of both financial embezzlement and administrative delinquencies. Corporate governance plays a vital role in the sustainability of the financial markets and thereby enhances the performance of the firms.

Corporate governance is receiving rapid adoption across the corporate culture of Pakistan. The corporate governance structure of Pakistan is ill-fated as compared to other developing countries. Nevertheless, the government of Pakistan is undertaking endeavors to enhance and evolve a strong corporate governance structure. After the execution of principles of corporate governance in Pakistan in 2002, fierce resistance was confronted by the corporate from the people due to compliance and cost-related issue (Chughtai, & Tahir, 2015).

The current challenge posed to the corporate sector is to vividly identify the role which should be adopted by corporate governance to ensure an increase in future stock return. Subsequently, understanding the relationship between corporate governance and stock returns in anticipating future stock returns is very crucial. Corporate governance is linked with the risks and several other unanticipated factors that are evident to predict the future stock returns in the financial markets (Afolabi, & Dare, 2015).

In Pakistan, most studies have been conducted on corporate governance but very few studies have been carried to investigate the impact of corporate governance on stock returns in the banking sector. In earlier studies, the major focus was concentrated on corporate governance in the non-financial sector while the present study is the first attempt to explore the association between corporate governance and stock returns in the financial sector. During the course of literature analysis, it was discovered that not a single study has investigated a comprehensive framework of several sub-factors of corporate governance affecting the stock returns in Banks with reference to Pakistan. Javed, Attiyya, and Iqbal (2006) conducted the association between corporate governance and firm performance, Iqbal & Kakakhel (2016) investigated the impact of corporate governance on profitability in Pharmaceutical Industry in Pakistan, Cheema, & Din (2013) investigated the impact of corporate governance on performance of firms, Masnoon, Maryam., and Rauf (2014) examined the impact of corporate governance on capital structure on the firms listed on KSE, Makki, Muhammad and Lodhi (2014) analyzed the impact of corporate governance on intellectual capital efficiency and financial performance, Latief, Raza (2014) studied the impact of corporate governance on the performance of privatized firms of non-financial sector of Pakistan, Iqbal, Muhammad, Javaid (2017) explored the moderating role of corporate governance on the relationship between capital structure and financial performance in the manufacturing sector of Pakistan, Onakoya, Ofoegbu, & Fasanya (2012) discovered the association between corporate governance and bank performance across the banking sector in Himaj (2014) explored the corporate governance in banks and its impacts on risk and performance based in Inam, Hifza, and Mukhtar (2014) probed the impact of corporate governance on the performance of banking sector in Pakistan, Zaman et al., (2014) appraised the role of corporate governance on firm performance in particular reference to the role of transparency and disclosure in banking sector of Pakistan and (Ghosh, Chinmoy, Huang, Di, and Petrova, 2016) evaluated the association between corporate governance and acquirer stock returns across the banking industry in USA. These facts established the gap within the literature regarding Pakistan and hence attempted to fill the existing gap by investigating the impact of corporate governance on stock returns in commercial public and private banks in Pakistan. This research is intended to achieve the objective; to examine the impact of corporate governance on stock returns in the banking sectors of Pakistan. This study contributes to the existing body of knowledge on corporate governance by providing real results of stock returns in public and private sector banks listed on the Pakistan Stock Exchange. Most

of the previous studies considered non-financial sectors and different aspects of corporate governance other than the ones considered in the present study. Ur Rehman & Mangla (2010) pursued a comparative study of Conventional and Islamic Banks in Pakistan regarding Corporate Governance and performance of financial institutions. The study provides first-hand knowledge to the public and private sector banks regarding specific aspects of corporate governance with stock returns which were overlooked by previous studies Cheema, & Din, (2013); Haque, & Tariq (2012); Javed, Attiya and Iqbal (2006); Mir, & Nishat (2004); Sajid, Muhammad, Nasir, & Farman, (2012) who studied corporate governance in both financial and non-financial sectors but with different dependent variables like firm performance, capital structure, agency cost, dividend policy, idiosyncratic stock returns, ownership structure, etc. The study will surely break the constraints to progression in academic research, education, and practice.

2. Literature Review and Hypothesis Development

2.1 Theoretical Evidence

In recent literature, the issue of corporate governance has got the substantial attention of researchers, academicians, corporate leaders, investors, and the general public. It has become an area of fierce deliberations for financial analysts, corporate professionals, and policymakers. Shahid, (2001) defined corporate governance as “the totality of rules by which the management is controlled and directed to increase the profitability and enhance the firm value for shareholders”. Sullivan, & Shkolnikov (2007) explained that corporate governance is related to establishing the structure and implementation of decisions undertaken by the board of directors.

With the increase in the growing complexities of modern-day businesses, the people have comprehended the significance of corporate governance for financial stability yet several companies in Pakistan are unwilling to adopt the principles of corporate governance. The Security and Exchange Commission of Pakistan (SECP) undertook the initial measures to enhance the structure of corporate governance and issued codes of corporate governance in March 2002. Similar preliminary initiatives were also taken by the Institute of Chartered Accountants of Pakistan (ICAP) for the enhancement of corporate governance mechanisms. It was declared in these codes that all listed companies are required to publish annual reports demonstrating their conformity with codes of corporate governance of Pakistan. These reports are reviewed by the auditors to affirm that the organization has complied with the principles of corporate governance (Kamran and Shah, 2014).

Fama & Jensen (1983) explained that stock markets as a whole are liquid and large when investors are protected. It is also argued that the diffusion of ownership has an impact on the profit maximization goal of the corporation. Because control separation enables managers to force their interests. Managers of a widely held corporation may be more averse than the block holder control corporations. According to Baums, and Scott (2003) “Corporate governance includes all those forces which influence the decision making of the firm. It encompasses not only the control rights of shareholders but also the control and insolvency powers of the debt holders. It also includes the commitment to employees, suppliers, and the customers, the statute, and the regulation. The firm decisions are powerfully affected by the competitive condition of the market in which it operates”.

Jensen, & Meckling (1976) explained that the relationship of agency denotes a business contract under which a principal party employs an agent party. The very agent party is empowered to undertake decisions on behalf of the principal party. Both the principal and agent are agreed to the agency bond via a written agreement. Gürsoy, & Aydoğan (2002) suggested that the problem of agency cost and separation of ownership & Control can only best be administered in the presence of effective

corporate governance. Dey (2008) analyzed that agency theory functioning with the effort to ensure effective corporate governance promptly overcome the problems associated with agency cost.

Donaldson, & Davis (1991) developed the Stewardship theory as opposed to agency theory. This theory assumed that the managers will perform as responsible stewards towards the assets they control provided if they are delegated a certain degree of freedom. Stewardship theory provides a substitute view to agency theory in which the agents act in their self-interest at the expense of the principal. Barney, & Hesterly (2010) recognized the nexus between personal needs and objectives of the firms. They further pointed out that personal needs are satisfied with collective choices of organizational performance. Nicholson, and Kiel (2004) held the view that managers safeguard shareholders and undertake decisions on their behalf. They assumed that an agent's performance and behavior were linked with the shareholder's objectives. They pinpointed that stewardship theory negates agency cost as managers remain reliable and dedicated. Siebels, & Knyphausen-Aufseb (2012) proposed that the stewardship theory is instrumental in ensuring effective and corroborative corporate governance. They identified that the management operating under stewardship theory within a firm is democratic, responsible, and conscious in improving the mechanism of corporate governance.

Freeman (1984) argued that stakeholder theory plays an important role in explaining the governance structure and practices. It highlights the interest of all shareholders and maximizes the profit. Firms under stakeholder theory are made responsible to be conscious of the interests of all stakeholders instead of mere equity holders. According to Post, Preston, & Sauter-Sachs (2002) Stakeholder Theory is a framework of dominated ethics in business and organizational management that addresses ethical values in the management of an organization. This theory was proposed by R. Edward Freeman in his book, "Strategic Management: A Stakeholder Approach". He is regarded as the father of the stakeholder theory. Typical stakeholders include employees, suppliers, consumers, government, shareholders, creditors, and communities encompassing the boundaries of a business's operations.

Resource dependency theory (RDT) was propounded by (Pfeffer, & Salancik, 2015). This theory analyzes the impact of environmental resources on organizational activities. This theory assumes that organizations depend on resources for their survival and activities derived from the environment of the organizations. RDT examines external resources of organizations such as expertise and capital that affect the organizations. Casciaro, and Piskorski (2005) suggested that organizations react to and depend on the entities which supervise the resources that are indispensable for their survival in an environment. Pfeffer (1973) highlighted that RDT stipulates several descriptions for practices through which the board of directors ensures functions that are required for financial firm performance. This theory is based on the assumptions such as (i) The Board of Directors ensures crucial resources such as knowledgeable decision and experience, (ii) The Board of Directors throws light on the interests of stakeholders, such as government, creditors, and employees. Hillman, Dalziel (2003) asserted that the composition of corporate governance structure i.e., the Board of Directors affects a firm's access to resources that are vital for the firm performance. Kaplan and Minton (1994) claimed that firms are required to hire efficient and renowned directors in situations when the firm financial performance is poor. Weisbach (1988) recommended that internal negligent directors must be substituted with external heedful directors. (Nicholson, and Kiel (2004) recognized that building a network with an external environment enhances the firm's values and performance.

Ritzer (2005) studied the process by which structures i.e., rules, regulations, norms become established as valid guidelines for social behavior. Scott, Richard, and Christensen (1995) underlined that it is mandatory for the survival of the organization to obey rules in the prevalent environment of

organizations. McKnight, Phillip and Weir (2009) described that institutional corporate governance has both internal and external governance mechanisms and juxtapose these concepts with institutional theory.

Chizema, & Buck (2006) elucidated that institutional theory has been related to path dependency. This theory has been executed as an explanation for the national system's divergence in international corporate governance. Major, & Hopper (2004) analyzed that organizational arrangements are adopted since external establishments favor them. Institutional linkages are not merely controlling techniques for connection of economic nature, but also rules and opinions and a source of legality. Scott, Richard, and Christensen (1995) established the enigma between market and institutional forces by restraining its privileges for governmental and non-governmental organizations.

2.2. Measurement of variables

2.2.1. Independent Variables

2.2.1.1. Board Size

Board size is a vital constituent of corporate governance and offers aid in enhancing the performance of the organization (Cadbury, 1992). It represents the total number of board size. Board size takes into account various issues pertinent to the affairs of the business. It undertakes various decisions for the banks on behalf of the shareholders.

2.2.1.2. Board Fraction

Board fraction signifies the composition of the board. It includes executives, non-executive directors, and independent directors. According to Weisbach (1988) independent or outside director monitors the actions of the executive director and make sure that he/she is not exploiting shareholders right.

2.2.1.3. Block of Common Shares

It is the percentage of common shares owned by financial institutions. This block includes banks (Conventional, Islamic, Investment, and Commercial), securities companies, mutual funds, insurance companies, and Mudaraba.

2.2.1.4. Individual and Family Block Holdings

It is the percentage of shares owned by individuals and family members of the CEO. The individuals include the spouse who owns shares within the firm.

2.2.1.5. Insiders Block holdings

It is the percentage of shares owned by insiders. Insiders are those shareholders who have 10% or more shareholding and have greater influence over the management. Sometimes, a single person or a family member can also be an insider shareholder.

2.2.1.6. Industrial Block holdings

It is the percentage of common shares owned by industrial banks. This block of shareholders measures the common share of one company held by another joint-stock or a public limited company.

2.2.1.7. Firm Leverage

According to (Weil, 2003) firm leverage or financial leverage is the ratio of debt to total assets. Firm leverage is comprised of shareholders borrowing money for securities investment. Firm leverage is expressed in percentage (Abdoli, Mohammadreza, Lashkary, Mohammad., and Deghani, 2012).

2.2.2. Dependent Variable

2.2.2.1. Stock returns

The dependent variable used in this study is Stock returns. These are the returns that investors make out of the stock market. These could adopt either the form of profit earned through trading or the dividend offered by the company to its shareholders (Brealey, Myers, & Allen, 2011).

2.2.3. Conceptual Framework

Independent Variables

Dependent Variable

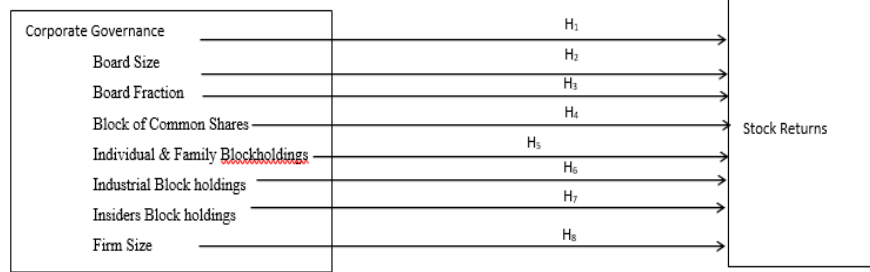


Figure 1. Conceptual Framework

2.2.4. Research Hypotheses

The theoretical framework extracted from the literature review leads to devise the following set of hypotheses for the present study:

H₁: Corporate Governance has a significant impact on stock returns.

H_{1a}: Board Size has a significant impact on stock returns.

H_{1b}: Board fraction has a significant on stock returns.

H_{1c}: Blocks of Common shares have a significant impact on stock returns.

H_{1d}: Individual & family block holdings have a significant impact on stock returns

H_{1e}: Insider holdings have a significant impact on stock returns.

H_{1f}: Industrial block holdings have a significant impact on stock returns.

H_{1g}: Firm leverage has a significant impact on stock returns.

3. Research Methodology

3.1 Nature, Population, Sample Sampling Technique, & Instrument development

The present study is empirical in nature and thus has attempted to analyze the financial data of the public and private banks covering the period 2016-2020. It has used descriptive statistics since the measurement of the variables is quantitative. This study has adopted a quantitative research approach as it is deductive in nature and aims to test theories and theoretical assumptions.

This research aimed to investigate the impact of corporate governance on stock returns. It examined the factors of corporate governance that impacted the stock returns of the firms listed on the Pakistan Stock Exchange from 2016 to 2020. Ten financial firms i.e., public and private sector banks are included in the sample. The research is mainly based on the secondary data acquired from annual reports of the selected banks, Pakistan stock exchange, and State Bank of Pakistan.

All Public and Private Commercial Banks listed on Pakistan Stock Exchange constitute the population of the current study. There are a total of 21 public and private sector banks that are listed on the Pakistan Stock Exchange as of 2016. The population includes only Public and Private Sector commercial banks. We have taken 10 banks as a sample of which 5 banks are private and the other 5 are public sector banks.

Purposive sampling technique has been used to collect the sample and the criteria fixed for the sampling is the top ten (10) banks that have exhibited outstanding financial performance in the banking sector as declared by State Bank of Pakistan for the year 2015.

This study is based on secondary data. The data of the pattern of shareholders, the board size, board fraction, firm leverage, and categories of shareholders are extracted from the annual report of the

selected banks and the Ministry of Finance. The share prices of each Bank for five years' period (2016-2020) have been taken both from the Pakistan Stock exchange and the "Open doors" website.

3.2 Method used for measuring results

Simple Linear Regression is used to analyze the data to find the impact of corporate governance on stock returns in Pakistan. Since the data of the present data is panel data, i.e., it is cross-sectional as well as time series simultaneously. The data is cross-sectional in the sense that it is taken from different banks originating from the public and private sector for a single period while it is time series in the context that it is based on a specific time period, i.e., 5 years (from 2016 to 2020). E-Views 8.0 software has been used to obtain the descriptive statistics results as well as the results of regression analysis. Moreover, the assumptions of regression analysis have been checked with SPSS that includes a normality test. Multicollinearity test, homoscedasticity test, and Normal distribution of error term test. JarqueBera test was also conducted to check the normality of all residuals of values using E-Views 8.0 software.

3.3. Econometric Model

This research tried to determine the impact of corporate governance on the stock returns of banks in Pakistan. We have used the following econometric model.

$$SR_{i,t} = \beta_0 + \beta_1 BSIZE_{i,t} + \beta_2 SOEXT_{i,t} + \beta_3 SOFIN_{i,t} + \beta_4 SOINDIV_{i,t} + \beta_5 SOINSD_{i,t} + \beta_6 SIINDUS_{i,t} + \beta_7 FTLEV_{i,t} + \epsilon_{i,t}$$

Where

BSIZE = Board Size

SOEXT = Board Fraction

SOFIN = Block of Common Share

SOINDIV = Individual & Family Block holdings

SOINSD = Insiders Block holdings

SIINDUS = Industrial Block holdings

FTLEV = Firm Leverage

$\epsilon_{i,t}$ is the error term

Stock Returns is computed using the following formula: (Fama, & French, 1992)

$$\text{Stock Return} = \frac{P_1 - P_0 + \text{Dividend}}{P_0}$$

Whereas

P_1 = Share Price at the end of a particular period

P_0 = share price at the start of the particular period

The dividend is the amount of cash paid to the shareholder at the end of the year

Table No 1. Measurement of the variables

Variable	Label of Proxy	Measurement & Description
Independent Variables		
Board Size	SIZE	Log of no. of board members. Dummy variable coded 0 if the board of director's members is not between 7-13 members and 1 otherwise.
Board Fraction	DEXT	ratio of outside director to the total number of directors. It is a dummy variable coded 0 If the board of directors is not controlled by more than

		0% independent outside directors and 1 otherwise
Block of Common Share	DFIN	percentage of blocks of common shares owned by financial institutions.
Individual & Family Block Holdings	BH	includes the shares owned by the individuals and their family members (spouses).
Block Holders	DINSD	the number of shares held by the block holders of the company, those who represent ownership of 10% or more. Dummy variable coded 0 if a shareholder-owned more than 10% and 1 otherwise.
Industrial Block Holdings	IBH	measures the common share of one company held by another joint-stock/ public limited company.
Firm Leverage	L	the ratio of total debt to total assets.
Dependent Variable		
Stock Return	R	is the ratio of net profit after taxes and preference dividends by the number of outstanding equity shares

4. Data Analyses and Results

Table 2 depicts the descriptive statistics of the variables included in the present study. It shows the values of mean, standard deviation, minimum, and maximum of all the variables used in the study. The sample consisting of 10 banks over the period 2016-2020. By analyzing the board size in the above table, the minimum and maximum level of board size is 4% and 18%. The average result of the board size is 9.7%. The average result of stock returns is 0.96 %. The Mean score for individual and family block holdings is 6.42%. While drawing a comparison among different sub-categories of the corporate governance utilized under the present study, the average score of individual & family block holdings confirms the notion that the majority of the firms in Pakistan are family ownership driven. The average result of the firm leverage is 0.89% which portrays the concentration of the assets held by the companies in Pakistan with the Banks.

Table No 2. Descriptive Statistics of Variables

Variable	Min	Max	Mean	Median	Std. Dev.
Board Size	4	18	9.7	10	3.4
Board Fraction	0.04	0.18	0.097	0.1	0.034

dividual & Family						
lock holdings	)	00	7.0	42	50	81
iders Block	)	00	42	60	56	89
ldings						
ustrial Block	)	19	09	60	56	89
ldings						
rm Leverage	)	26	96	87	89	10
lock of Common	)	97	1.5	79	94	07
ares						
ock Returns	)	51	15	96	93	81

Table 3 accounts for the projected results of regression analysis and validates that Board Size has a significant impact on Stock Returns as designated by ($t= 1.914906$, $p= 0.0498$ ($p<.05$)) and recognized by the value of $B=0.096393$. The results confirmed that board size is positively connected with stock returns. The alternate hypothesis is accepted and the null hypothesis is rejected because the p-value is less than 0.05. So consequently, the deviation in board size can bring change in stock returns. Board fraction is negatively associated to stock returns as represented by ($t= 0.049052$, $B= 0.096393$, $p= 0.7346$). The p-value is greater than 0.05 i.e., 0.7346. On the source of the above significance level, the null hypothesis is accepted and the alternate hypothesis is rejected. Therefore, it is recognized that board fraction will not bring change in stock returns.

The regression outcomes acquired for Block of Common Shares are; $t= 1.985902$, $B=2.371534$, $p=0.0472$). These results indicate a significant effect on stock returns the alternate hypothesis is accepted while the null hypothesis is rejected since the p-value is less than 0.05. It is exposed that, the individual & family block holdings have a positive impact on stock returns with as certified by $t= 2.067708$, $B= 0.013498$, $p= 0.0379$. The alternate hypothesis is accepted and the null hypothesis is rejected. The analysis exposed that insider's block holdings are negatively related to stock returns so there is no impact on stock returns. The result is demonstrated by $t= -0.678199$, $B= 0.000378$, $p= 0.5014$). The results validated the positive effect of industrial block holdings on stock returns as sustained by $t= 0.124241$, $B= 0.000390$, $p= 0.9017$ so, the null hypothesis accepted and rejected the alternate hypothesis.

There is found a negative association between Firm leverage and stock returns which is showed by the values; $t= 1.770625$, $B= 2.421010$, $p= 0.0893$). Hence, approves a positive impact of firm leverage on stock returns.

Table No 3. Regression analysis results

Independent variables	Coefficient	Std. Er	t-statistics	sig.
Constant)	146	413	518	1364
Board Size	096393**	049052	914906	0498
Board Fraction	024837	072768	341312	7346
Block of Common Shares	371534**	194185	985902	0472
dividual and Family				
lock holdings	013498**	006528	067708	0379
iders Block holdings	000378	000558	678199	5014
ustrial Block holdings	000390	003135	124241	9017
rm Leverage	421010*	367319	770625	0839

Dependent Variable: Stock Return

***, **, * indicate the significance at 1%, 5% and 10% level respectively.

Table 4 displays the results of Variance Inflation Factor (VIF) which detects the problem of multicollinearity. Mayer, Nishii, Schneider, & Goldstein (2007) explained that the Multicollinearity test is conducted to investigate the strength of correlation among variables. The existence of strong multicollinearity among variables obstructs to obtain precise results. The criteria for determining the multicollinearity varies among different scholars. Hair, Black, Babin, Anderson, & Tatham (2006) suggested a value of 5 be considered as a value providing the non-existence of multicollinearity while Mayer, Nishii, Schneider, & Goldstein (2007) proposed the value of VIF as 10.

In our present study, all the independent variable's VIF value is less than 5 except board fraction. Therefore, we can contend that there are no such serious issues of multicollinearity in our variables of interest.

Table No 4. Multicollinearity Test

Variables	Tolerance Value	VIF Value
Board Size	85	062
Board Fraction	69	933
Block of Common Shares	96	527
Individual & Family Block holdings	63	797
Insiders Block holdings	78	093
Industrial Block holdings	96	436
Firm Leverage	24	082

4.1. Discussion and Conclusion

The results are found consistent with the previous studies of David, Kochhar, and Levitas, (1998); Sanda, Mikailu, Garba (2005) who found a positive impact of board size on stock returns. The results contradict the work of Holthausen, and Larcker (1993) who found a negative impact of board size on stock returns with inconsistent evidence of association. The findings of the study are further endorsed by Cadbury (1992); Pathirawasam, & Wickremasinghe (2012) who found similar results.

The results of the study indicated a negative association between insider block holdings and stock returns which supports the results of King, & Segal (2003) who found a negative association between insider block holdings and stock returns. The results of the study are inconsistent with the findings of Demsetz (1983) who found a positive association between insider block holdings and stock returns. The study results complimented previous studies of Jensen, & Meckling (1976); Mehran (2001) who found a positive and substantial association between a block of common shares and stock returns. The results substantiated a positive impact of individual and family block holdings on stock returns. The results of the study are similar to the findings of (Mir, & Nishat, 2004) who concluded that the individual and family block holdings have a positive impact on stock returns.

The results of the study recognized a negative association between industrial block holdings and stock returns. The results conform to the findings of Barca, Fabrizio, and Becht, (2002); and (Pound, 1992) who confirmed a negative impact of industrial block holdings and financial institutions on stock returns.

The results exhibited a negative impact on firm leverage on stock returns. The results are in line with the prior studies of Dimitrov & Jain (2006); Korteweg, (2004); Lev, and Penman (1990) who found a negative association between firm leverage and stock market returns. The findings of the study

endorse the results of Adamia (2010) who examined the impact of firm leverage on stock returns and observed a negative association between the two.

The overall purpose of the current research is to develop an understanding of the impact of corporate governance on stock returns. The study was conducted to investigate the impact of corporate governance on stock returns of 10 banks from the public and private sector listed on the Pakistan Stock Exchange during the year 2016-2020.

The findings indicated that good corporate governance practices help a firm to increase its stock returns. This research further recognized that certain aspects of corporate governance i.e., Board Size, Block of Common Shares, and Family & Individual Block holdings are positively associated with stock returns. The results further suggest that an increase in the number of board members, common shares, and shares held by family members will lead to expansion and an increase in stock returns hence this association was found statistically significant.

The results of the research discovered a negative association of Industrial block holdings, Insider block holdings, and firm leverage with stock returns. It, therefore, accepted three alternative hypotheses for board size, a block of common shares and family & individual block holdings while accepted null hypothesis for board fraction, industrial block holdings, insiders block holdings and firm leverage which validates that among the corporate governance specific factors, these factors are negatively associated and therefore inflict no impact on stock returns.

Several prior studies have also supported the findings of this research and found that corporate governance has a significant impact on stock returns. The findings that are found inconsistent with previous literature are due to the criteria set for the firms selected and analyzed. The study suggested that the corporate governance mechanism has a significant impact on stock returns since it resolves agency costs. The results also support the findings of (Aivazian, Ge, & Qiu (2005) who investigated the impact of firm leverage on stock returns and found an insignificant impact.

5. Limitations, Future direction of the research,

One of the main limitations of the present study is its sample size of 10 banks. The researcher used purposive sampling to select these banks. The criterion was fixed to select only those banks that have demonstrated the highest profitability in the financial year 2015. The study has only considered commercial banks and therefore has excluded the investment banks and Securities and Exchange Commission companies listed on Pakistan Stock Exchange Pakistan. The current study is restricted to five-year financial data of public and private sector banks from 2016 to 2020. Data collection was a laborious job and therefore it was time-consuming. The researcher confronted sheer difficulty in acquiring the data for certain variables and approached different financial institutions. This limitation restrained the researcher to de scope the financial data covering only five (5) years.

The present study examined the internal mechanism of corporate governance while future research may consider exploring the external mechanism of corporate governance. Further studies should consider a larger sample size with a representation of different sectors other than the banking sector. Future studies should examine corporate governance with other sub-factors such as board disclosure & transparency, director's remuneration, ownership concentration, corporate and financial reporting with equity returns, idiosyncratic stock returns, firm-specific returns, trade volume, etc. The present study might be extended by a future researcher to other stock exchanges of the world by pursuing a comparative study of the corporate governance practices among different financial and non-financial firms. Future researchers may consider investigating the impact of corporate governance and stock returns between conventional and Islamic banks listed on the Pakistan stock exchange.

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