

## **Corporate Governance and Organisational Effectiveness in the Manufacturing Industry**

**<sup>1</sup>Bako, Yusuf A. & <sup>2</sup>Olabimtan, Rashidat O.**

*Department of Business Administration and Management,  
Federal Polytechnic, Ilaro, Ogun State*

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### **Abstract**

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Corporate governance is a matter of vital concern for all corporations, large or small, publicly traded or privately held. It is a combination of corporate policies and best practices adopted by the corporate bodies to achieve their objectives in relation to their stakeholders. The objective of the study was to investigate the effect of corporate governance on organizational effectiveness. The study adopted a survey research design where data was collected using a structured questionnaire. The study population comprises of 500 of Sona Agro Allied Foods Ltd, Sango Ota, Ogun State. The sample size of 119 respondents was chosen for the study. Data was analyzed through SPSS using Ordinary Least Square (OLS) while the hypotheses were tested using Multiple Regression Analysis. The findings of the study revealed there is a weak positive relationship between all the variables of corporate governance (board size, board composition, governance structure, management compensation structure) and organizational effectiveness. The study recommended that organizations should see corporate governance as a business opportunity that is profitable in the long run, which will give a clearer view of the ultimate goal of organizational success.

**Keywords:** *Corporate Governance, Organisational Effectiveness, Board Size, Board Composition, Management Compensation Program.*

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*Corresponding Author:*      **Bako, Yusuf A.**

### **Background to the Study**

It has become a worldwide dictum that the quality of corporate governance makes an important difference to the effectiveness and ineffectiveness of organizations. Corporate governance is defined as the way in which companies are directed and controlled in the interest of shareholders and other stakeholders (Agyei-Mensah, 2016). The term corporate governance describes the system by which companies are directed, controlled and made accountable to shareholders and other stakeholders. Broadly speaking corporate governance refers to the organizational governance of a corporation (McGrath & Whitty, 2015), thus, effective corporate governance practice incorporates transparency, openness, accurate reporting and compliance with statutory regulations among others. Historically, antecedents indicate that financial crisis is a direct consequence of lack of good corporate governance in organizations; invariably one of the sources of instability in the Manufacturing sector is inadequate practice of corporate governance.

### **Statement of Problem**

The challenging task facing policy makers is to design corporate governance frameworks that are secure, of benefit to all shareholders at large and as effective monitor of management whilst preventing them from extracting excessive private benefits of control (Amer, 2014). Mismanagement, bureaucracy, wastage, pilferage incompetence and irresponsibility by directors and employees are the main problems that make organizations fail to achieve their objectives (Adekunle & Aghedo, 2014). Corporate governance has assumed a central place in the continued effort to sanitize corporate reporting and shore up public confidence in achieving stated objectives of organizations around the world. The issue seems to revolve around putting the right rules, regulations and incentives in place to ensure confidentiality and accountability in the management of the affairs of corporate entities. However, organizations plan to improve on the mechanism of corporate governance which will help increase the effectiveness of the organization. This interest appears more appropriate at this time, when business executives and auditors are continually being held to higher standards of accountability. Corporate governance is viewed as an indispensable element of market discipline and this is fueling demands for strong corporate governance mechanisms by investors and other financial market participants (Abdulazeez, Ndibe and Mercy, 2016).

### **Objective of the Study**

The main objective of this study is to examine the effect of corporate governance on the effectiveness of Sona Agro Allied Foods Ltd.

In order to achieve the broad objective, the following null hypotheses were synthesized:

- H01:** There is no significant relationship between governance structures and organizational effectiveness.
- H02:** There is no significant relationship between management compensation programs and organizational effectiveness.
- H03:** There is no significant relationship between board composition and organizational effectiveness.
- H04:** There is no significant relationship between board size and organizational effectiveness.

## **Conceptual Review**

Corporate governance is the process carried out by the Board of Directors, and its related committees, on behalf of and for the benefit of the company's Shareholders and the other Stakeholders to provide directions, authority and oversights to management. Corporate governance represents methods through which organizations are being administered, a structure which the welfare of different parties with vested interests are harmonized, showing group of interaction between a company's administration, its shareholders and other interested parties (Cheema and Din, 2013). This is in a corollary with the argument that change or improvement of corporate governance practices should be consistent with surrounding value and the corporate environment as the context of implementation (Jamal and Waqas, 2018). Organizational governance represents a noteworthy variable that establishes the strength of the organization and the company's capability to live through financial shake-ups and the overall focus of organizational governance has to do with developing reliability, guaranteeing openness and responsibility.

In the last few years, the widespread realization of globalization and privatization has led to exponentially rising businesses across globe and thus inviting tremendous business communities to explore opportunities. Multinational companies with well-established corporate policies have improved the performances of the organizations. Corporate governance encompasses the regulatory paradigms and various management associated roles and responsibilities, organizational structure including functional and non-functional executives, Board of Directors and Stakeholders. It facilitates the operating guidelines that significantly intend to enhance the cumulative business prospects so as to attract stakeholders' trust, long term capital and productivity. As such, Wahyudin and Solikhah (2017) argued that Corporate Governance Perception Index could increase public trust, as well as confidence of investor and creditor to put their money in a company. Particularly, in case of the globalization and the privatization, maintaining optimal corporate governance is compulsory, as it is affected significantly due to numerous internal as well as external attributes. In spite of such globally anticipated and widespread interest, exploring evidence that corporate governance influences firm performance and associated value often remains an open research domain across global economy.

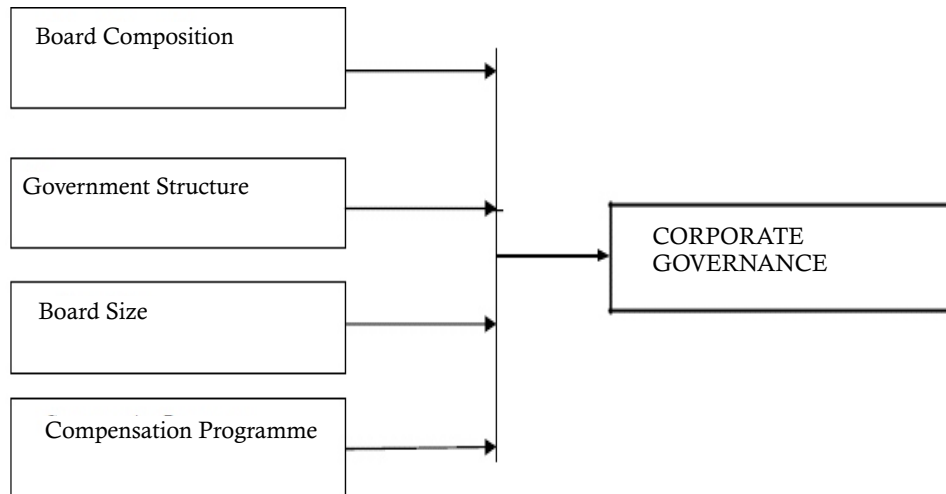
Corporate Governance is a broad concept and not easy to describe due to continuous expansion of the boundaries of the concept. The definition may vary based on the different perspective of researchers. However, some of definitions of Corporate Governance are generally classified into value creation indicates that developing the long term goals for sustainable performance by focusing on the shareholders of the company and value protection which is accomplished through corporate governance (Adekunle and Aghedo, 2014), value protection is based on accountability of managers and protects the interest of both shareholders and stakeholders (Ajagbe and Ismail, 2014). Also, most researchers argue that definition of organizational performance is incorporated with effectiveness and efficiency, Santos and Brito (2012) state “business performance or firm performance is a subset of organizational effectiveness that covers operational and financial outcomes”. Organizational effectiveness is a broader construct that captures organizational performance, as

organizational effectiveness is defined as the efficiency with which an organization is able to meet its objectives. This means an organization that produces a desired effect or an organization that is productive without waste. Exploring in depth, Corporate Governance can be stated as the structure as well as the process by which a company is managed with intent to enhance its business prosperity and responsibility, so as to ultimately improve and ensure wealth creation for the allied stakeholders. In general, there are both internal as well as external variables affecting Corporate Governance and amidst those variables; ownership pattern, control structures and the organizational setup do primarily influence the firm performance (Dina, Ivana and Marina, 2014).

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**Fig. 1:** Components of Corporate Governance



**Components of Corporate Governance (Adopted from Cross, Bazron, Dennis & Isaacs, 1989)**

1. **Governance Structure:** the board of directors represents the membership of the organization. The board sets in place policies, procedures, values and long term planning to meet the mission of the organization and the board do this through a governance model.
2. **Board Composition:** it is concerned with issues related to board independence (including independence of board committees), diversity (firm and industry experience, functional backgrounds, etc.) of board members, and CEO duality.
3. **Compensations Programs:** it is the components of a compensation packages (wages, salaries, and benefits), the manner in which it will be paid, and for what purpose employees receive bonuses, salary increases and incentives.
4. **Board Size;** it refers to the total number of directors on the board of each sample firm which is inclusive of the CEO and Chairman for each accounting year. Saravanan (2012) research work in India on manufacturing firms shows that size of board and performance has positive significant relationship.

**Relationship between Corporate Governance and Organization Performance**

According to the Business Dictionary, performance is the accomplishment of a given task measured against present known standards of accuracy, completeness, cost, and speed. In contract, performance is deemed to be the fulfillment of an obligation, in a manner that releases the performer from all liabilities under the contract. It connotes successfully outcome and does not just entail putting in some efforts (Fekri, Milad, Hafezali, Alaeddina and Omer, 2016). Performance therefore is a multidimensional construct, the measurement of which varies depending on a variety of factors, according to Bilal, Shahid, Muhammad, Hafiz and Arbab (2013), Firm performance is an important concept that relates to the way and manner

in which financial resources available to an organization are judiciously used to achieve the overall corporate objective of an organization, it keeps the organization in business and creates a greater prospect for future opportunities.

Performance management (PM) is a set of activities that ensure goals are met in an effective and efficient manner. Performance management can focus on the performance of an organization, a department, an employee, or the processes in place to manage particular tasks. Performance management standards are generally organized and disseminated by senior leadership at an organization, and by task owners. Performance management is the term used to refer to activities, tools, processes, and programs that companies create or apply to manage the performance of individual employees, teams, departments, and other organizational units within their organizational influence. In contrast, performance appraisal refers to the act of appraising or evaluating performance during a given performance period to determine how well an employee, a vendor or an organizational unit has performed relative to agreed objectives or goals, and this is only one of many important activities within the overall concept of performance management (Fekri, Milad, Hafezali, Alaeddina and Omer, 2016).

At the workplace, performance management is implemented by employees with supervisory roles. Normally, the goal of managing performance is to allow individual employees to find out how well they had performed relative to performance targets or key performance indicators during a specific performance period from their supervisors and managers. Organizations and companies typically manage employee performance over a formal 12-month period (otherwise known as the formal company performance period).

### **Relationship between Corporate Governance and Corporate Image**

In order to understand the influence of the corporate image on the organizations, different views about the essence of this organizational attribute are necessary to be considered. The corporate image can be defined as the sum of impressions that the stakeholders (such as customers, shareholders, suppliers, employees and the society) have about the organization. The good corporate image should be able to align the understanding that the organization has for itself of “who we are”, with the feeling that remains in society with its activities (Erhardt, Werbel and Shrader, 2013). All the positive aspects of the good corporate image can be combined in the concept of “brand equity”, which result in more loyal customers, more productive workforce and higher profitability. The corporate image is built from positive corporate figures, marketing communications and channels and constant feedback from the public and the stakeholders (Duc and Thuy, 2013).

The positive corporate image provides clean relations between the organization and the stakeholders, recognition from the consumers and increasing loyalty and reputation among the employees. The corporate image becomes a competitive advantage because inherently it builds the image of the brand in the minds of the consumers, which is established over a long period of time and is difficult to be imitated or emulated (Jamal and Waqas, 2018). The positive corporate image can increase the sales and the customer loyalty and can attract new investors and employees that could invest their potential and knowledge in the organization.

### **Relationship between Corporate Governance and Organization Effectiveness**

Organizational effectiveness is the concept of how effective an organization is in achieving the outcomes the organization intends to produce; Jamal and Waqas (2018) reminds us that effectiveness can and must be learned. Organizational Effectiveness groups in organizations directly concern themselves with several key areas, they are talent management, leadership development, organization design and structure, design of measurements and scorecards, implementation of change and transformation, deploying smart processes and smart technology to manage the firms' human capital and the formulation of the broader Human Resources agenda.

### **Corporate Governance and Firm Profitability**

Financial theories on the connection between corporate governance and firm financial profitability are based on equilibrium asset pricing models as well as on the efficient market hypothesis. It predicts three possible relations. One direction of reasoning postulates a neutral relation. It assumes that the risk associated with compliance with Corporate Governance is not priced, therefore all companies Corporate Governance complying as well as non-Corporate Governance complying, have the same rate of expected return and face the same cost of equity capital (Khalid and Muhammad, 2013). This reasoning is in line with standard financial theory (risk-return paradigm) where only risk factors are priced in the market. On the other hand, if the risk associated to Corporate Governance compliance is (correctly) priced by the market, the same risk-return paradigm would imply a negative relation between Corporate Governance and financial performance (Juliet, Aduda, Gituro and Mwangi, 2016).

### **Theoretical Framework**

#### **Agency Theory**

Agency theory propounded by Stephen Ross and Barry Mitnick stipulates that the ownership and control of firms are vested in different individuals; there exists a conflict of interest between principal and agent (Juliet, Aduda, Gituro and Mwangi, 2016). According to Williamson (1975), managers may seek to fulfill their own self-interests as opposed to shareholder's interest or worth. Thus, managers cannot be trusted, even though they are often thought to be rational. In line with this school of thought, Jensen and Meckling (1976) assert that managers do not constantly pursue shareholders interest, and corporate governance is therefore an effective tool in solving the agency problem with the establishment of board.

Agency theory is widely used as a means of explaining various corporate governance issues. The essence of the theory is based on the existence of separation of ownership and control in large corporations. In such corporations, the managers (agents) are hired to work and make decision on behalf of the owners (principals) in order to maximize return to the shareholders. However, conflict of interest between the agent and the principal inevitably occurs when the agent fails to act in the best interest of the principal, and instead act to maximize their own value. Such conflict of interest occurs due to difference in their preferred level of managerial effort, their attitude towards risk, and their time horizons, which in turn may lead to divergence in the goals of managers and shareholders. Consequently, different control mechanisms either internal or external to the firm should be put in place in order to align the

interests of managers and shareholders. Nevertheless, argue that, assumptions made in agency theory about individualistic utility motivation resulting in principal-agent interest divergence may not hold for all managers; and therefore, exclusive reliance on agency theory is undesirable, because the theory ignores the complexities of organizational life.

### **Stewardship Theory**

Theodore Roosevelt propounded the stewardship theory. Stewardship theory views manager as the guardian of shareholders' investment and the guardian is taking the companies' assets in order to fulfill their higher needs of achievement and self-actualization (Donaldson and Davis, 1991). The executives of the companies hold a view that they are attached to the existence of companies, and the reputation of companies is also their reputation. Consequently, this perspective viewed that the interests of shareholders and managers are aligned, since there exists insignificant conflict of interest among parties due to the assumption of the theory. The stewardship theory originates from sociology and psychology. The stewardship theory maintains that managers are not motivated by individual goals but rather they are stewards, whose motives are aligned with the objectives of their principals-shareholders; as opposed to the agency theory which claims that conflict of interest between managers and shareholders is inevitable unless appropriate structures of control are put in place to align the interests of managers and shareholders. The stewardship perspective suggests that stewards (managers) are satisfied and motivated when organizational success is attained even at the expense of the stewards' personal goals. Furthermore, while the agency theory suggests that shareholder interests will be protected by separating the posts of board chair and CEO, the stewardship theory argues that shareholder interests will be maximized by assigning the same person to the posts of board chair and CEO to give more responsibility and autonomy to the CEO as a steward in the organization.

### **The Stakeholder's Theory**

Edward Freeman propounded the stakeholder theory. This theory states that the firm is a system of stakeholders operating within a larger system of the society which provides the required legal and market infrastructure for the firm to thrive. The purpose of the firm in this case is to serve the general public who may have direct or indirect relationship with the firm. The management and the provision of information should be directed at satisfying the interest of the general public rather than shareholders.

### **Empirical Review**

Sicily Gachoki and Gladys Rotich (2013) examined the influence of Corporate Governance on the Performance of Public Organizations a study of Kenya Ports Authority (KPA). Corporate governance in Kenya has been an important topic because of corporate scandals such as the recent complaints on the composition of the board members in the state corporations against the tribal lines basis. Albeit a lot of literatures have drawn much emphasis on the relationship between corporate governance and ownership and on the relationships little is known about the influence of the corporate governance on performance of public organization. The factors considered include; Board composition, Management compensation, Governance structure and Board size. Out of the four variables studied it was found that the board composition had a greater influence on the performance of public organizations.



Danquah, Gyimah, Afriyie and Asiamah (2018) studied the relationship between corporate governance and firm performance an empirical analysis of some listed manufacturing firm in Ghana. Specifically, the paper investigated whether gender diversity, board independence, and board size affect return on asset (ROA) and return on equity (ROE). The results showed that board independence and return on equity (ROE) have positive significant relationship at 1 percent significance level. Thus, the existence of outside directors in terms of their strict supervision, advice, expertise in financial, legal and other areas and their external influences positively affects the financial performance of manufacturing listed firms in Ghana. This means that as the number of non-executive director's increases, manufacturing firms tend to perform better. The empirical results again showed that gender diversity has a positive significant relationship with ROE at 1 percent significance level. Also, there is no statistical relationship between board size and ROE and there is no link between board size and firm performance.

This implies that the size of boards today does not really matter, however the caliber of people on the board is a matter of importance since board independence and gender diversity had a significant influence on the firm performance.

The significance of corporate governance has been argued commonly among public listed firms without paying attention to specific industries. The paper emphasizes on the importance of corporate governance in the manufacturing sector of Ghana. We find that board independence and gender diversity of boards have positive significant effect on the performance of manufacturing listed firms in Ghana. The researchers generally suggested that the implementation of corporate governance principles has some imperative implications for manufacturing firms in Ghana. The study notes that board independence ensures better management practices through boards exerting much needed pressure, greater opportunities, stronger internal auditing, and strategic outlook through external directors. Williams, Chukwuma and Anthony (2016) the paper examined the impact of corporate governance on performance of manufacturing firms in Nigeria. The empirical findings revealed that Chief Executive Officer Shareholding has a positive and a significant impact on organizational performance at 5% level of significance. Director's shareholding has a negative and a significant impact on organizational performance at 1% level of significance at 1% level of significance. Board gender has a negative and an insignificant impact on organizational performance at more than 10% level of significance. On the basis of these findings, the study recommended excerpts that increase in Chief Executive Officer Shareholding would significantly improve organizational performance. It was also recommended that increase in Director's Shareholding would significantly lead to a decrease in organizational performance.

Tanko and Kolawole (2015) found out that there was a high relationship between the boards size of the companies used in the study and their performances. On board composition, the study found out that averages of 30 percent of all board members are outsiders which suggested that these boards are relatively not independent. They therefore showed a weak relationship in that direction. The study concluded that the more outsiders there are on a

company's board, the better the performance in terms of return on equity. On CEO to serve as the chairman of the company, the study found out that when a CEO also serves as the board chairman performance worsens.

Delima and Regel (2017) provide that board size and code of conduct have not significantly contributed to organizational performance. It can be suggested that board of directors have to concentrate on their roles to lead the organization successfully. Meanwhile, financial institutions have high level of organizational performance. Thus, these institutions have more concentrated on customer satisfaction and employee commitment. But financial institutions fail to concentrate on corporate reputation. Hence, they should focus on risk of investment and also future growth of companies.

### Methodology

This study adopts quantitative research design under the survey research method. The population of Sona Agro Allied Foods with 502 employees at all the three levels of management including top level, middle level and lower level of management and this was obtained during the collection of information on the number of employees in the organization.

Taro Yamane technique was used to determine the sample size.

$$\text{Thus } n = \frac{N}{1 + N(\varepsilon)^2}$$

Where:  $n$  = Sample size

$N$  = Population (502 staffs)

1 = Unity (a constant)

$\varepsilon^2$  = level of significance

$\varepsilon$  = 0.07 or 7%

$$n = \frac{502}{1 + 502(0.07)^2}$$

$$n = \frac{502}{1 + 502(0.0049)}$$

$$n = \frac{502}{3.45}$$

$$n = 144.9275$$

3.45

$$n = 144.9275$$

Approximately 145

Primary data employed in this study was collected using a structured questionnaire. Secondary data is collected from available books, publications, research studies, articles and internet.

Multiple regression analysis was used to examine the relationship between corporate governance and organizational effectiveness with the aid of statistical package for social sciences (SPSS).

**Table 1.**

Cronbach's Alpha 0.842	Valid Number 119	Number of Items 20
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**Source:** Author's Computation, 2019.

The above shows the reliability of the questionnaire used for the survey research. This shows the Cronbach's alpha of 0.842 which is an indication that the questionnaire used for the research work is highly reliable. Hence further analysis can be done on the result obtained from the field.

### Results and Discussion

**Table 2a:** Summary of result of hypotheses

Statistics	Values
<i>Multiple R</i>	0.204
<i>R-squared</i>	0.042
<i>Adjusted R-squared</i>	0.007
<i>F-value</i>	1.213
<i>Standard Error</i>	5.778
<i>p-value</i>	0.009

**Table 2b:** Summary of result of hypotheses

Variable	Regression Coefficient	Standard Error	t	Sig
Constant	10.369	1.232	8.416	0.000
GS	0.014	0.106	0.135	0.003
BC	0.017	0.094	0.185	0.004
BZ	0.021	0.049	0.438	0.002
MCP	0.285	0.131	2.170	0.032

Level of significant  $p \leq 0.05$

**Source:** Author's Computation, 2019

### Discussion of Results

The result of the analysis as indicated in table 2a shows that there is a weak positive relationship between joint effect of board size, board compensation, governance structure and management compensation programs on organizational effectiveness with regression coefficient of 0.204. Furthermore, it is noticed that about 4.2% variation in organizational effectiveness is attributed to board size, board compensation, governance structure and

management compensation programs. It also revealed that the joint effect of the independent variable will on account for about 0.7% variations in organizational effectiveness with the inclusion of new independent variables. However, the F-value is 5.778 with significant value of  $0.009 < 0.05$  significance level.

Furthermore, the contribution of each independent variable (that is; board size, board composition, governance structure and management compensation programs) is as indicated in table 2b above. The gradient of the regression line is 10.369, which is the contribution in the absence of the independent variables to organizational effectiveness. In addition, in the absence of other three independent variables, the regression estimate for governance structure is 0.014 with standard error of 0.106 and t-value of 0.135. Similar result is obtained for board composition which has regression coefficient of 0.017 with standard error of 0.094 and t-value 0.185. Furthermore, board size has regression coefficient of 0.021 with standard error of 0.049 and t-value of 0.438. Lastly, the regression coefficient of management compensation programs is 0.285 with standard error of 0.131 and t-value of 2.170.

Consequently, it is observed that all the four independent variables are significant with their respective significant values of 0.003 for governance structures, 0.004 for board composition, 0.002 for board size and 0.032 for management compensation programs. This is an indication that all the variables are significant and hence we accept the alternative hypotheses, that is: there is significant relationship between management compensation programs and organizational effectiveness for hypothesis one. There is significant relationship between management compensation programs and organizational effectiveness for hypothesis two. There is significant relationship between management compensation programs and organizational effectiveness for hypothesis three and there is significant relationship between management compensation programs and organizational effectiveness for hypothesis four.

The overall performance of the model is as indicated by the F-value of 5.778 with p-value  $< 0.05$ . This result indicates that the model is adequate and sufficient in relating the dependent and the independent variables.

The model for the research work is given as:

$$\text{OREF} = 10.369 + 0.014*GS + 0.017*BC + 0.021*BZ + 0.285*MCP$$

Where,

OREF represents organizational effectiveness

GS represents governance structures

BC represents board composition

BZ represents board size

MCP represents management compensation programs

From model (1), the result indicates that every unit increase in governance structure will lead to 1.4% increase in organizational effectiveness provided other independent variables are held constant. In addition, for every unit increase in board composition, there exists 1.7% increase in organizational effectiveness provided all other independent variables are held constant. In the same vein, for every unit increase in board size, there exists 2.1% increase in organizational effectiveness provided other three independent variables are held constant. Lastly, for every unit increase in management compensation program, there exists 28.5% increase in organizational effectiveness. This result shows that; management compensation program contributes more to the organizational effectiveness than other variables.

### **Summary and Conclusion**

The study objective was to explore the effect of corporate governance on the effectiveness of manufacturing firms. The study established that there is weak positive relationship between joint effect of board size, board composition, governance structure and management compensation programs on organizational effectiveness. Consequently, it is observed that all the four independent variables are significant to organizational effectiveness, accepting that board size, board composition, governance structure and management compensation programs have positive significant relationship with the effectiveness of the organization. This result indicates that the model is adequate and sufficient in relating the dependent and the independent variables. This result shows that management compensation program contributes more to the organizational effectiveness than other variables.

It can be concluded from the study that there is positive weak relationship between corporate governance and effectiveness of Sona Agro Allied Foods Ltd. It is also concluded that corporate governance components (board size, board composition, governance structure and management compensation programs) contributes to the effectiveness of the organization, but it is concluded based on the result that management compensation program contributes more to the organizational effectiveness than other variables. The study concludes that sufficient evidence emerged showing that it is necessary to embark on good management compensation program which supports the organization in achieving better effectiveness.

The study recommends among others that corporate governance requires more attention and commitment from corporate organizations in the formulation of custom, policies and laws so as to provide a guide and channel efforts towards the use of effective corporate governance in achieving organizational success. The organization should adopt effective management compensation programs which aid the employees in doing the right things that will help to improve effectiveness. Corporate organizations should also intensify efforts to ensure that the governance structure supports the effectiveness of the organization and that the Executive directors are placed in handling the affair of the organization since they have a deeper understanding of the organization operation. Organization should ensure that all board members should have relevant industry knowledge, qualifications, experience and skill required in stewarding the organization which will improve the effectiveness of the organization.

Finally, organizations should see corporate governance as a business opportunity that is profitable in the long run. This will give them a clear view of the ultimate goal of organizational success.

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