CAPITAL UNIVERSITY OF SCIENCE AND TECHNOLOGY, ISLAMABAD

An Empirical Examination of the Impact of Country Level Governance on Profitability of Pakistani Banks

by

Wajiha Shakoor

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This work is dedicated to my beloved parents, teachers, and friends for their valuable support.

CERTIFICATE OF APPROVAL

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(Wajiha Shakoor)

Abstract

The purpose of the study is to evaluate the impact of country-level Governance on the profitability of Pakistani Banks. In this regard the sample of commercial banks use from the year 2006 to 2019. The study employs panel data regression analysis by using fixed effect model. Three main indicators are used to test the profitability Return on Equity, Return on Assets and Net Interest Margin. The results reveal that country-level Governance has a significant impact on profitability of Pakistani banks. This study presents novel evidence related to country level governance to the profitability of Pakistani banks. The findings provide guidance to banks and fulfill the gaps of existing literature. As banks are the main financial intermediaries in Pakistan. Hence its operations affect economy. Therefore, this study demonstrates how the banks can operate in such a way to maximize their profits. This study also bridges the gap in the body of literature on profitability and country level governance of Pakistani banks.

Keywords: Country Level Governance, Profitability, Financial Intermediaries , Fixed Effect Model.

Contents

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Abbreviations

CAP	Capital
CPI	Corruption Perception Index
CGI	Corporate Government Index
CRAR	Capital to Risk-Weighted Asset Ratio
DEP	Deposit
FSA	Financial Statement Analysis
IMF	international Monetary Fund
ISS	Institutional Shareholder Service
LN	Loan
OECD	Organization Economic Cooperation and Development
NIM	Net Interest Margin
ROA	Return on Assets
ROE	Return on Equity
R&D	Research and Development
SZ	Size

Chapter 1

Introduction

1.1 Background of the Study

The sector of banking is performing a main role in resource mobilization. Lack of trust on other financial systems and underdeveloped capital market has made the banks most dominant financial intermediary in Pakistan. Banking sector of Pakistan encompasses of commercial banks, foreign banks, Islamic banks, development financial institutions and microfinance banks. Ownership of banks in Pakistan is varied including state owned, foreign controlled and family owned. Due to these reasons many emerging economies implemented policies for banking sector. The efficiency and profitability of banks in Pakistan have followed similar reform policies as in 1990s. Part of these policies includes best performance known as "governance of banks"(Khalid & Hanif 2005). Scholars laid stress on governance practices as it is necessary for the reduction of risks for investors and it also help for enhancing performance of companies (Wakaisuka-isingoma et al., 2016)

The legal environment and regulatory processes of each country are constituted by governance level of that country's schemes and it creates cooperation as well as involvement between private and public sectors. Zahra (2014) documented that governance practices of a country directly influence the legislation guidelines as per country-level such as audit performance. Thus Country-level governance in this era is becoming a major concern for the regulators, academicians, policymakers as well as for the investors around the globe. Even the terminology of "Country-Level Good Governance" is acceptable in academic literature since 1990s and is becoming more and more popular day by day. (Ngobo&Fouda, 2012). The indicators developed by the World bank are more popular and frequently used around the world (Bot et al., 2018). Studies highlighted the usage of these indicators by describing in two ways. In number of countries around the world their use is more frequent. For that a complex model of comparison is provided by these sub sets has become of great opportunity for them (Bot et al., 2018). The comprehensive approach is the second advantage by these indicator is as it has derived from combining different "views of a large number of enterprises, citizen, and expert survey respondents in industrial and developing countries. It is based on over 30 individual data sources produced by a variety of survey institutes, think tanks, non-governmental organizations, international organizations, and private sector firms. As the report of World Bank 2019 stated that "The Worldwide Governance Indicators of the World Bankreports"aggregate and individual governance indicators for over 200 countries and territories over the period 1996 up to 2017".

Banks performed under the good governance showed good performance as documented by Mishra and Mohanty (2014) Good performance of accompany can attract investors and other potential users and lead organization to high values as it's a fundamental point of view however, the poor performance can become the reason of lowering share values of company. The efficiency of a firm and effectiveness are the reflection of the performance of that company (Kusuma&Ayumardani, 2016).

Banks in Asian countries are evolving and emerging from last couple of decades (Sinha& Sharma, 2016). However, number of other financial institutions are also operating which includes both types of banking as well as non-banking sector (Ghosh, 2016). Country level governance has become a great interest spot for policymakers, regulators, investors and academicians nowadays. As prior literature has stated that since 1990s country level governance has become more prominent in academic (Ngobo and Fouda , 2012). Bota-Avram,(2013) stated that for having a sound business environment, governance is one of the most important pillar and is main stream concern for all over the world. Moreover, Bundschuh-Rieseneder

(2008) has defined country-level governance as the "favorable political structure and conditions for ecological, social and market-oriented development which is responsible for rational use of public resources and political power by the state". Nevertheless, six country level governance indicators was also developed by The World Bank for academicians and their use is most common in academic as narrated by Boţa-Avram et al.,(2018). These worldwide indicators as narrated in World Bank reports as The Worldwide Governance Indicators (WGIs) "aggregate and individual governance indicators for over 200 countries and territories over the period from 1996 up to 2017" (The World Bank, 2019).

For fair regulatory frameworks, legitimacy, justice, sovereignty of law, market openness, transparent and accountability a better governance is important to maintain as it ultimately leads to better economic activity, sound business environment (Avram, Grosanu&Rachisan, 2015).most of studies have been conducted on country level governance and profitability in other countries. Some of the literature is also available on the impact of country level governance and entrepreneurship (Álvarez&Amorós, 2014; Amha&Ageba, 2006; Avnimelech et al., 2011; Jiménez &Alon, 2018; Kim et al., 2015; Ngunjiri, 2010; Shagbazian&Aistov, 2017). However the impact of country level governance on entrepreneurship is determined by different dimensions as narrated by (Álvarez&Amorós, 2014; Dheer, 2017; Goltz et al., 2015; Groşanu et al., 2015; Kim et al., 2012; Shagbazian&Aistov, 2017; Tabares, 2017). With this reference Fredström et al. (2020) revealed that the productivity and entrepreneurship is significantly got affected by the quality of strong governance.

However, the current research demonstrate the effects of country level governance on bank's profitability in Pakistan. It mainly demonstrates the profitability being affected by country level governance on banks of Pakistan in general. Further it evaluates issues by considering the type of banks separately as in private and public banks. And finally by considering the effect of demonetization of Pakistan and to predict the effect of country level governance on their profitability. Studies in past has been conducted on country level governance and its influence on profitability of firms in several countries around the globe. But the indicators used to examine vary from country to country, thus the outcomes of prior researchers are not applicable in the scenario of Pakistan as the culture of Pakistan is different from these counties. Hence in the context of Pakistan the research is not sufficient especially ever since the policy of demonetization has been applied. The current study will mainly focus on the issues of political, accountability and rule of law as faced by Pakistani Banks. Hence, the foreign banks, non-performing assets and competition of non-banking sector under the influence of political leaders have faced major challenges in Pakistan. Moreover, frauds have been witnessed in most of the banks of Pakistan. Thus this study will highlight major challenges facing by Pakistani banks and their effect on profitability.

The current research is in quest to make contribution, significance and to provide practical implications. The gap of existing literature regarding country level governance is needed to be filled thus this study will fulfil that. However there are few studies that demonstrated this issue are in some other countries. But due to difference of economic factors this will fill that gap. Moreover the academicians and investors will find practical implications from give research. By considering the demonetization and bank types of Pakistan the current study will address the effect of country level governance on profitability by examining statistical approaches for assessing scientific contributions.

In firms, presence of strong governance mechanism is mainly responsible for investments of investors. As studies investigated that confidence of investors about the firm is not linked to self-interested managers but it is dependent on strong governance of firms. And it is observed especially in public listed firms. The reason behind in this is that the resources and capital provided to the public firms are mainly outside investors. Their survival depends on investments by outsiders and that‘s why it is considered as the life blood for their growth. Berle and Means‘s investigated in their seminal work , in context of this is, outside investors mostly do not get any advantage especially in the case when they do not have any resource to get access to information for the future prospects of firms or any other source to monitor inside of firms operations. Along with it they also mentioned that especially when they have no expertise in it. So in this case it depends on quality of governance maintained in the firm. Because the good governance can guarantee that the firm‘s mechanism is improved and it is a prove of validity of accountability. Furthermore they also suggested that good governance points out that financial information of firm and its efficiency of the capital market is reliable and it enhances investors' confidence and ultimately increased returns in stock market. However, all most of the theories assumed that investors are rational but empirical studies provide evidence that investors are not always rational and can be impulsive and make wrong investment decisions in stock market. Certain factors can compelled them in lead to wrong decision in stocks. (Dorn, 2009 and DeLong, Shleifer, Summers, &Waldmann, 1990).

Thus a number of studies have found that decisions of firms managers highly influenced investors' confidence. (e.g.Polk&Sapienza, 2009; Gilchrist, Himmelberg& Huberman,2005; Baker & Wurgler,2004). So in result investors views about firms become more optimistic and they tend to invest more when their confidence enhances about the firm and when the stock returns become higher the investors optimism about firms gets higher too. It all results when the firm maintained good governance. The empirical study which include the sample of 398 firms Korean, Malaysian, Indonesian, Philippines, Thailand taken by Mitton (2001) have found that during East Asian Crises in 1997 and 1998 a strong influence of on firm performance by the variables such as firm-level differences and governance has been investigated. The results of these studies shows that firms those have has indicators of higher disclosure quality, they are more focused as compare to firms those are diversified and they have higher outside ownership concentration show better performance in price and stock market returns. However, the firms of US as examined by Brown and Caylor (2004), they analyzed 51 factors of US firms, 8 sub-categories for 2327 firms based on dataset of Institutional Shareholder Service (ISS). From analyzing these firms they suggested that firms with better governance are relatively more valuable, better satisfy their shareholders in financial aspects, their overall stock returns are high and are relatively more profitable. In addition to this, Lipton and Lorsch (1992) investigated that firms who maintained limited board size improve their performance in stock market because large group board size along with its benefits have problems related to monitoring. Including this oversized board also has poorer communication and delay of decision making. Jansen (1993) also investigated it that outweighed board size results in poor performance of firms because of poor communication.

The way in which an organization is administered, directed or controlled is referred to as governance. This term includes certain set of rules and regulations that contribute to the system in which current and potential stakeholders are perceived by the company along with it governance also affects the manager‘s decision. The rights and duties of board of directors, managers, shareholders and all stakeholders are specified by coporate governance in a firm. It specifies the rules and procedures and also provides certain assistance in decision making assistance on important corporate affairs. The concept of governance for corporation is a structure base as it offers the structure through which a firm ‘s goals are defined and set, along with it, it also provide means of getting those objectives. governance defined the ways to monitor the performance. Firms are meant to work for the benefits of its stakeholders so as far as governance is concerned the firm with governance can bring into line the interests of managers and its investors so both get benefits without conflicts. governance make capital of the firm effectively occupied and mobilizes efficient use of resources in larger economies and within the companies. A company‘s financial performance and good governance is influenced by the size of board of directors examined by Adestian and Nuswantoro (2014). More studies about governance and stock returns also conducted in the markets of Germany (Drobetz et al., 2004). European markets and UK (Bauer et al., 2003). However Ammann et al. (2011) founded results on base of 22 different countries and suggested a positive influence of governance on firm‘s value. La Porta et al (2002) examined that since controlling stakeholders tend to seize from minority stakeholders in an environment with a smaller amount of investor protection particularly in the evolving markets, the more valuable intangible asset is considered as if the firm is practicing governance.

In regard to poor governance of Pakistan, as estimated by World Bank: the government effectiveness index as well as the regulatory quality index was observed negative from last two decades. For these consistent negative effects of Pakistan are told to be influenced by a lot of factors in for governance its corporate environment. One of the factor was observed by scholars is foreign influence on governance. Foreign influence on governance was one of the factors that were observed. In addition to this literature past literature showed that the influence of International Monetary Fund (IMF) has greatly influence Pakistan from its origin and some of other funding agencies too. Other reasons as were mentioned by researchers for poor governance of Pakistan is that Pakistani economy is plagued with more corruption as compare to other Asian countries. One of the report published by Transparency International that Corruption Perception Index (CPI) which should be 100 if there‘s no corruption, in the case of Pakistan it never cross 30. That is the reason for poor governance and including executives people in Pakistan are more inclined to opportunistic and unethical performance. (Mujtaba & Afza, 2011).

Ammann et al. (2013), measured the interactive consequences of quality of governance and market competition used a dataset from fourteen European countries and he suggested that in non-competitive industries good governance increased firm‘s value. Hence, the relationship of market competition and good governance is significantly positive. Furthermore findings of other researchers in same area such as Giroud and Mueller (2011) and Ammann et al. (2013) investigated that effects of competitive market competition in industries forces managers to stay disciplined therefore, it is suggested that product market competition play a role of auxiliary for governance.

Country level governance practices are primarily vary from country to country and it is well known that these practices are vary at firm level. Doidge, Karolyi, and Stulz (2007), Some of researchers illustrated that to find some specific dterminents for country level governance is quiet hard so in result determinants for country level governance has remained a puzzle. Thus according to prior researchers subject of country governance has two limitations. First there are countries which largely focus on governance practices where there is transparency, equity pay based and independent board systems and they defined it as “good” by influential international organizations including the Organisation for Economic Co-operation and Development (OECD) and the World Bank, securities regulators, proxy advisory firms, and governance rating agencies. These are labeled as governance Eng as it portrays “one-size-fits-all” solution to agency problems in a firm. This one size fits all mainly suggest a common set of governance practices for all firms and that should be adopted and implemented by all firms in a specific country.

Studies conducted in this context among firms operated in Europe and East Asia by Shleifer and Vishny (1997) have observed that the firms situated in Europe and East Asia , tend to adopt the direct control approach of governance from their investors. Some of the examples are relational banking, pyramid structure and concentrated ownership in this regard. This is so the ratings used in this paper for the governance and in prior literature proved to be an effective measures for the two governance approaches. The two approaches of governance namely the Anglo-Saxon approach and the direct control approach.

Moreover the governance models that exist in the control power of the firm remains constant so this constant effect make the decisions of firm level governance‘s reflection of tradeoff for the lessening of cost and capital (Doidge, Karolyi, &Stulz, 2004, 2007; Francis, Khurana, & Pereira, 2005; Durnev& Kim, 2005; La Porta, Lopez-de-Silanes, Shleifer, &Vishny, 2002; Shleifer&Wolfenzon, 2002). Furthermore the controller of the firm will improve firm-level Country level Governance only if the cost of capital effect more than offsets the insider's loss in private benefits.

Legal protection of shareholders is one of the major factors relevant to this first tradeoff. Strong legal protection of shareholders makes improvement of firm-level CG more economical for the firm controller in the first tradeoff, because 1) it provides more support for the enforcement of firm-level governance and 2) the firm controller has less private benefits to lose under strong legal protection. The first tradeoff therefore suggests that legal protection should explain most of the cross-country variation in firm-level Country level Governance (Shleifer&Vishny, 1997).

However, studies also reveal that the failure of legal protection, together with the development of economic and financial has empirically explain on the governance. Hence the governance of a firm depicts the choices for firm and country level governance. The control rights of a firm is rooted in the primary goals of the governance over contingencies in managers and stakeholders (Shleifer&Vishny, 1997).

Moreover it is necessary to protect the interests of investors and for this the retention of residual rights or direct approach to control of a shareholders can become possible. As this approach is certainly providing control over self-dealings of manager but here the decision making power of major shareholders under this approach is not certified here hence, the benefits of expertise by managers can be lose. For that reason the hiring of managers at first place is the first priority of managers. The governance practices such as board independence, performance-based compensation, financial disclosure and shareholders voting is under the approach of Anglo-Saxon and that relies on all of the above mentioned practices as it mainly allows monitoring and managerial direction. On the bases of manager's expertise the current approach provide managers more discretion. But the cost of uncertainty of shareholders entails the loss of control. The prior literature has largely overlooked the second tradeoff. Researchers mentioned that this second tradeoff is more interconnected with the preferences of a country as for the direct approach comes in versus with Anglo-Saxon approach. The contribution in international finance literature by the researchers is huge till now. Different from previous literature on country level governance and culture the scholars with a conceptual framework observes some direct effect of culture on country level governance of firms. However the effects of culture on country level governance has been observed indirectly it the association of country level governance is with culture namely as legal systems of a firm (Licht, Goldschmidt, & Schwartz, 2005). Literature conducted on country level governance and culture revealed that the effects of culture are direct and the effects are equally being strong no matter if there are other institutions to control it. In addition to this the two dimensions of culture namely uncertainty avoidance and individualism has completely captured the fixed effects of country on its governance and their effects on culture. However scholars also stated that it is not the reason that its association with country level governance indicators.

Nevertheless a number of studies therefore offer a solution to the puzzle of "why countries matter so much for firm-level governance" (Doidge et al., 2007). The impact of national culture on country level governance of firms are strong and it has explanatory power too, hence prior literature revealed a mechanism for from which the effect of national culture operates which are tradeoff among certainty of control and managerial expertise. Moreover the tradeoff has more overlooked by prior literature that mainly influence the cultural values of country level governance decisions. The residual control rights among shareholders and managers are based on the essential purpose for the country level governance as for the second tradeoff (Shleifer&Vishny, 1997). However, the relation of first tradeoff for the need of governance that how much is required but the second one relates to which framework of governance should be used. Literature also provided evidence for the second tradeoff's validity and revealed that the interaction of this indeed with more than 7 essential tradeoff frameworks for examining the country level governance around the globe. The importance of second tradeoff for international level governance is suggested by the results of second tradeoff as it provides an alternative frameworks to guide for future.

Third, a number of studies revealed that results the reason for adoption of different governance mechanism by different countries. The reason is that the ratings of indicators of country's governance is different on priority lists in every country especially in Anglo-Saxon versus the direct control approach. The agency problem however as described in prior literature raise here between these two general approaches (Shleifer&Vishny, 1997); moreover the U.S and U.K like counties go for the Anglo Saxon approach in contrast to this Germany and Japan like countries tend to follow direct control approach. Through relationship of governance existing literature revealed the influence of country level governance, corporate cash flows and stock returns to investigate that in efficient market stock returns is highly affected by governance. They further argued that to prevent managers from diverting resources and impedes their efforts for value creation of firm its necessary to have better governance in the roots. It also results not only to change the likely cash flow but along with it the risk-return trade-off stock investors.

For building sustainable and long run business good governance is more vital to consider as evidence from corporate finance literature shows that good governance and the level of product market competition affect the stock returns. Several other existing studies have also described the relation between governance, stock returns and product market competition. As Sias and Starks (2006), investigated the nexus between stock returns volatility and governance and find that good governance produce better results of firm's stock returns. However, Gompers et al. (2003), Drobetz et al. (2004), Bebchuk et al. (2008), and Ammann et al. (2011) has empirically proved the theory that for gaining better profits and enhancing firm vale good governance practices are vital to operate, moreover a good relationship between governance and stock returns is rather period-specific is suggested by Core et al. (2006). The relationship of market competition and governance by Gompers et al. (2003) suggested that regarding their effects on stock returns in less competitive industries poorly governed firms showed their equity returns with lower values along with lower firm value with worse operating performance.Thus findings suggested that firms in highly competitive industries get less benefit with good governance than firmsin less competitive industries. Better governed firms have higher stock returns. (Gompers et al.2003). The practices of governance affect the firm‘s stock returns.

However difference in profitability of better and poorly governed firms is investigated by Core et al. (2006) is in significant in Korean markets. Other researchers argued that the correlation amid governance and firm‘s returns are explained by investor learning effects from these results that after the investors come to know that how important is the governance for the firm then the abnormal stock returns of firm even with food governance decreases and ultimately firm‘s profitability decreases with poor governance practices. (Bebchuk et al., 2013). A company‘s financial performance and good governance is influenced by the size of board of directors examined by Adestian and Nuswantoro (2014). More studies about governance and stock returns also conducted in the markets of Germany (Drobetz et al., 2004). European markets and UK (Bauer et al., 2003). However Ammann et al. (2011) founded results on base of 22 different countries and suggested a positive influence of governance on firm‘s value. La Porta et al (2002) examined that since controlling stakeholders tend to seize from minority stakeholders in an environment with a smaller amount of investor protection particularly in the evolving markets, the more valuable intangible asset is considered as if the firm is practicing governance.

With contrast to this some other researchers for example, Ryu et al (2014) examined no significant association between stock market returns and product market competition in Korean markets. Moreover, results from the studies of Gallagher et al, (2015) showed effects of industry concentration in the Australian markets, they suggested that stock returns in firm are higher in less competitive industries than those in more competitive industry firms. He further argued that firms are able to make monopoly rents in less competitive industries. Hence there are contrast results in Korean, U.S and Australian markets as far as the relationship between product market competition and stock returns remain concerned. However some other researchers conducted their studies in western world and investigated that they are in contrast with Asian countries as stated by Fan et al., 2011, Ghosh, 2006, Gibson, 2003, Hofstede, 1980, Sun et al., 2010, van Essen et al., 2012, that the settings related to institutions and behavioral distinctiveness are not same in all over the world and they varies from socio-economic systems of Asia to throughout western world. They also mentioned in their studies that all researches that were conducted in Western world are not implacable in Asian countries as socio-economic system of Western world and Asian countries are totally different. In this context we see that in Pakistan the situation is more opposite as stated by Rehman et al., (2012) that Pakistan in its legal and political environment is too weak as compare to other countries, moreover Overall governance of Pakistan is also poor.

In regard to poor governance of Pakistan, as estimated by World Bank: the government effectivenessindex as well as the regulatory quality index was observed negative from last two decades. For these consistent negative effects of Pakistan are told to be influenced by a lot of factors in for governance its corporate environment. One of the factor was observed by scholars is foreign influence on governance. Foreign influence on governance was one of the factors that were observed. In addition to this literature past literature showed that the influence of International Monetary Fund (IMF) has greatly influence Pakistan from its origin and some of other funding agencies too. Other reasons as were mentioned by researchers for poor governance of Pakistan is that Pakistani economy is plagued with more corruption as compare to other Asian countries. One of the report published by Transparency International that Corruption Perception Index (CPI) which should be 100 if there‘s no corruption, in the case of Pakistan it never cross 30. That is the reason for poor governance and including executives people in

Pakistan are more inclined to opportunistic and unethical performance. (Mujtaba and Afza, 2011). Moreover, a few more suggestions in alternating explanations to this suggested that industry concentration and high profit have positive relationship. Furthermore concentrated industry shows higher returns although they are more risky. Supporting this argumentSubrahmanyam and Thomadakis (1980) developed hypothesis on empirical evidence in their studies. Moreover,Sullivan (1978, 1982),Bernier (1987) and Lee et al. (1990) also give their argument in support of this hypothesis.

A lot of studies discussed about market concentration and innovation by taken proxies about expenditure on research and development (R&D) and has shown relationship among them on industrial organization. Moreover, a lot of studies exist on accounting and finance that linked the channels of studies firm‘s expenditures on R & D and their respective stock return/market value of equity. However most latest work on firms expected returns are conducted by Lev and Sougiannis (1996), Chan et al. (2001), Kothari et al. (2002) and Penman and Zhang (2002). They investigated that firms show higher stock returns when they are more concerned about their R&D. Intensive R&D results excessive stock returns. In addition to this R&D activity of firms is highly affected by product market structure of fir thus it is clearing indicating the link between a firm‘s stock returns and its product market structure.

The empirical study which include the sample of 398 firms Korean, Malaysian, Indonesian, Philippines, Thailand taken by Mitton (2001) have found that during East Asian Crises in 1997 and 1998 a strong influence of on firm performance by the variables such as firm-level differences and governance has been investigated. The results of these studies shows that firms those have has indicators of higher disclosure quality, they are more focused as compare to firms those are diversified and they have higher outside ownership concentration show better performance in price and stock market returns. However, the firms of US as examined by Brown and Caylor (2004), they analyzed 51 factors of US firms, 8 sub-categories for 2327 firms based on dataset of Institutional Shareholder Service (ISS). From analyzing these firms they suggested that firms with better governance are relatively more valuable, better satisfy their shareholders in financial aspects, their overall stock returns are high and are relatively more profitable. In addition to this, Lipton and Lorsch (1992) investigated that firms who maintained limited board size improve their performance in stock market because large group board size along with its benefits have problems related to monitoring. Including this oversized board also has poorer communication and delay of decision making. Jansen (1993) also investigated it that outweighed board size results in poor performance of firms because of poor communication.

Other researchers such as Yermack (1996) analyzed that firm‘s performance in Stock market, asset utilizations and board size of frims has inverse relationship, it also includes profitability. Good governance also improve financial accounting processes as documented by Anderson et al. (2004) that the cost of debt is much less for larger boards, because creditors when view that firms are monitoring effectively their financial accounting progressions. Kinney, et al. (2004) investigated that earnings restatements and fees paid for financial information systems have no association between them and their implementation including internal audit services. Firms earn huge market returns to book ratios with director stock options along with as firms discloses its stock option plans it is because when it earns more profits and have a positive market reaction for their directors. Furthermore, good monitoring of firms when maintained then investors show positive reactions and they tend to invest more as stated by La Porta, et al (1999) the willingness to invest by investors increased when they feel protected and the firm‘s legal environment seemed to be stronger. In addition to this Meckling(1976) argued that a basic conflict between shareholders and managers in context to governance always remain at some extent. While having other goals by managers the first and fundamental of a corporation is to give returns on the investments of shareholders, while other objectives are likely to run larger organization‘s power and prestige, such as power and prestige of running larger and dominant organizations, monitoring, amusement and some other privileges associated with their position. Researchers such as Fama and Jensen, (1983) investigated that the access of managers as upper hand is more likely as in the situation where managers have more access t0 information inside the organization.

A company‘s financial performance and good governance is influenced by the size of board of directors examined by Adestian and Nuswantoro (2014). More studies about governance and stock returns also conducted in the markets of Germany (Drobetz et al., 2004). European markets and UK(Bauer et al., 2003). However Ammann et al. (2011) founded results on base of 22 different countries and suggested a positive influence of governance on firm‘s value. La Porta et al (2002) examined that since controlling stakeholders tend to seize from minority stakeholders in an environment with a smaller amount of investor protection particularly in the evolving markets, the more valuable intangible asset is considered as if the firm is practicing governance.

With contrast to this some other researchers for example, Ryu et al (2014) examined no significant association between stock market returns and product market competition in Korean markets. Moreover, results from the studies of Gallagher et al, (2015) showed effects of industry concentration in the Australian markets, they suggested that stock returns in firm are higher in less competitive industries than those in more competitive industry firms. He further argued that firms are able to make monopoly rents in less competitive industries. Hence there are contrast results in Korean, U.S and Australian markets as far as the relationship between product market competition and stock returns remain concerned. However some other researchers conducted their studies in western world and investigated that they are in contrast with Asian countries as stated by Fan et al., 2011, Ghosh, 2006, Gibson, 2003, Hofstede, 1980, Sun et al., 2010, van Essen et al., 2012, that the settings related to institutions and behavioral distinctiveness are not same in all over the world and they varies from socio-economic systems of Asia to throughout western world. They also mentioned in their studies that all researches that were conducted in Western world are not implacable in Asian countries as socio-economic system of Western world and Asian countries are totally different. In this context we see that in Pakistan the situation is more opposite as stated by Rehman et al., (2012) that Pakistan in its legal and political environment is too weak as compare to other countries, moreover Overall governance of Pakistan is also poor.

The governance of a firm and agency theory is inter-related. The agency theory stated that managers of firm with poor governance can easily pursue private benefits but not to those managers of frims with good governance (Core et al. 2006; Gompers et al. 2003; Giroud and Mueller 2011). However, poor governance practices firm's manager's face less competition. By keeping it in view it has been investigated that good governance can lessen agency problems to arise with stakeholders and that also affect profitability of the firm. Analyses form markets of other countries such as U.S market Giroud and Mueller (2011) suggested that equity returns of firms are observed lower with poor governance practices by the firms and their operating performance is also seemed poor. They also investigated that firm‘s value is not good if they have weak governance practices. This is the reason of firm‘s agency problem as it faces less pressure and results in weak governance practices.

1.1.1 Impact of Financial Crises on Pakistan Banking Industry

The financial crises of Pakistan greatly influenced the financial institutions and mainly banking sector. Currently Pakistan has faced serious crises in the domains of current account deficits along with higher inflation rates it also faces lower reverse volume, poor currency scenario and a breakable economy that raised the risk to face Pakistan financial problems worldwide. As far as macroeconomic situation of Pakistan is concerned the administration is trying to tighten the fiscal and monetary procedure. The world economic crises tells us that there is no more non-financial foreign capital spread. Its influence on country‘s own banking sector would be its subunits therefore there is possibility of more pressure analysis that recommends the commercial bank area in overall. It suggests to resist the fluctuations. Based on past innovation it is probably estimated that it is the recovery of the financial health by financial institutions. The financial crises faced by the world were not in favor of Pakistan and it expand it to a higher level extent. A major fall in the foreign exchange reserve level was the reason of collapse in balancing payments as examined by the government, hence foreign investments in millions went down in session 2008 to 2009. The trade collapse in Pakistan increased 12.8% as in GDP ratio as the world economic crises widened. However, in November 2008 for the purpose of avoidance of defaulting foreign level debt payments, a well managed program established by Pakistan required by IMF was introduced.

The economic instabilities in Pakistani culture was initiated during the period of 2007 and 2008 when the rapid increase in oil prices was occurred and resulted a huge economic instability in Pakistan. The examination of macroeconomic determinants of Pakistan elaborated the very poor performance of Pakistan because of the reason of gross domestic expansion level and by putting financial positions at the risk. Moreover the world‘s economic crises highlighted the focus of economists to several other problems. They revealed that there are requirements for knowledge in economy. For having a better economic structure around the world IMF required knowledge and information.

To maintain financial and economic integration in Pakistan there is a requirement to initiate a section for the world economic market. Hence, the impact and fluctuations of the worldwide downfalls were also needed to be examined that are not predicted. The trading balance has also given influenced the progress of globally trade. It lower the requirements of worldwide and also the prices of commodities.

The word bank is extracted from two EUROPEAN and Italian word BANCO. The word BANCO means a counter or customer. Banks are financial institutions that meant to deak with money and credits. Regularized commercial banks of Pakistan are main sources of financial institutions in Pakistan that includes foreign, national and private level financing including both banking and non-banking. These kind of financing involve finance division, leasing investments, mordarabas and real estate finance firms. For retaining extraordinary success banking sector in Pakistan has grown in success and work harder. In profit making organizations conventional banks do not operate on religious principles. These are based on manmade laws assume to be unethical. Their main purpose is to generate more income through interests. On the other hand Islamic banks are based on ethical principles for that interests are prohibited. Prior researchers argued that Islamic banks actually reflects the principles of conventional banks namely the operating aspects. Here it generates the argue that most of the Islamic banks are not founded on the principles of Shariah which are the right principles of Islamic banking systems. (Aggrawal & Yousaf, 1999). In theory it is stated that the role of Islamic banks is not as the conventional banks because of the prohibition of interest. To ensure the legitimacy of the investors that he deposited money must be used in real investments.

The major distinguish among conventional and Islamic banks are the profits and interests. The transactions in Islamic banks must be based on real investments and do not involve any of the transaction on haram investments such as sale of alcohol etc. moreover speculations are also not considered in it. They also not suppose to carry debts on behalf of others such as Pakistani stock markets. Companies whose debts are less than 30% are eligible and then finally the companies like Murhabah and Musharkah.

1.1.2 Supporting Theory

According to Santos (2000) the related theories of banks suggest that banks from the difference between lending and borrowing interests lend money from the difference of interests' rates. However the functions performed by Islamic banks are similar to them but the difference is that in Islam interest is strictly forbidden. So Islamic banks used profit maximization theory so they can guide their clients that there are no fixed rates for interests in Islamic banking sector. The agreements are bases for profit earning for depositors along with borrowers. Without interest the earning of profit is the stream of Islamic banks.

1.2 Problem Statement

Studies in past has been conducted to evaluate the impact of country level governance on profitability of banks in several countries. Most of the research regarding governance is conducted in developed countries henceforth there is a need to conduct similar research in banks of under developed countries. (Ryu.,etal. 2017). Moreover, country level governance is different from country to country and the results from the studies of conducted around the world may not be applicable in the context of Pakistan. Therefore the purpose of the current study is to examine the role of country level governance on profitability in banking sector of Pakistan.

1.3 Research Question

1. Does the country level governance affect the profitability of banks?
2. Does the capital has positive effect on banks profitability?
3. Does the deposits has positive effect on banks profitability?
4. Does the loans has positive effect on banks profitability?
5. Does the size has positive effect on banks profitability?

1.4 Research Objective

1. To find the effect of country level governance on profitability of banks.
2. To examine the effect of capital on banks profitability.
3. To examine the effect of deposits on banks profitability.
4. To examine the effect of loans on banks profitability.
5. To examine the effect of size on banks profitability.

1.5 Significance of Study

Effective governance mobilized the effective use of company resources. It also attracts the low cost investors as well as international investors. As banks are more important financial sources in Pakistani economy where capital market is not so stable therefore it is vital for banks to maintain effective governance. Good governance makes sure accountability of managers and board of directors. The risks in banking sectors were further exposed by crises occurred in Latin America, Asia and Europe from 1980s to 1990s. In the sample countries of given paper some of the crises might lead to recession, major bankruptcies and in some cases to economic and political instability. The emerging economies of these countries have high non-performing loan ratios, thus it is considered more essential to develop a country level governance code for the banks. In consideration of these views it is considered an essential and more basic need in an emerging economy and a valid focus fir research to develop governance for banks (Khalid & Hanif 2005). .

Chapter 2

Literature Review

The banking sector in an economy, serves the main source of resource mobilization. From last couple of decades the role of banks as an intermediary of finances is dominant in most of the countries where Pakistan is one of them. This is due to the reason of underdeveloped money market and capital structures. Along with it lack of confidence on financial instruments is also the dominant reason in Pakistan. From last couple of decades Pakistani banks have performed very well. Undoubtedly contribution of banks in economic progress of Pakistan is hardy to exaggerate. Soon after its independence in 1947 the banking system which was inherited by Pakistan was foreign. At start of 1951 only 97 branches of domestic banks were operating there, but the condition of today is quite different as 98% of banks in Pakistan are domestic banks (Yao et al. 2018). A number of banking reforms were introduced after this remarkable growth from last couple of decades.

However, when Pakistan government was nationalizing all domestic banks the industry suffered a setback in 1947. Along with this government issued licenses to private banks after realizing the need alongside with the national banks. Pakistan government also took number of reforms to avoid adverse consequences and to update banks industry (Hardy and di Patti 2001). Prior researchers suggested that to navigate the banking industry and to make it more competitive those reforms were mandatory to be taken by eliminating operational inefficiencies as stated by Patti and Hardy (2005). As in Pakistan there were a lot of challenges related to higher risk exposure, hogher financial cost, and credit restrictions so the reforms slowly influenced on the growth and performance of banks (Akhtar 2006).

In contrast to this, form last decades there has been a significant improvement. Which was as determined by (Yao et al, 2018) from 2007 to 2016 the increase in total assets were seen by 413 %, increase in equity by 215 %, bank deposits increase by 299 %, advance increased by 160

Prior researches from time period 2005 to 2012 examined that the relationship among BI rate, in this one of the variable is taken as interest rate taken from central bank of Indonesia and the second variable taken was profitability and taken from the conventional banks registered in the Stock exchange of Indonesia form the use of NIM and ROA for the proxy of profitability. The investigation found that the policy rate of these proxies has negative effect on ROA, however the current study proved statistically that they do not found any significant effect on profit margins of net interest. Further studies investigated that policy rate has the correlation coefficient and large effects in return of equity ranks determinations. However, in addition to this the significance of functioning cost here is large for determining margins of net interest in the banking systems of conventional banks of Indonesia.

For this many emerging economies develop some policies so banks can perform their intermediary role with more stability. However, banks in south Asian countries have been following reform policies since 1990s to make banking system more efficient and profitable. Similarly Pakistan has also adopted some policies to improve its operations. Country level governance was designed as guidelines for performing best practices.

2.1 Country Level Governance and Profitability:

The term “Country level governance” has been recognized in academic literature since 1990s and from then it has become so popular (Ngobo&Fouda, 2012). However, The World Bank developed some common indicators for country level governance and those indicators have become more popular in worldwide. “World-wide Governance Indicators” provided by the World Bank has two advantages when is practically implemented as studies has determined, the first one is the use of these indicators by several countries across the earth, hence it gets a benefit in a way that country gets opportunity to develop a sub-set and intricate comparison model for its operations. (Bota et al. 2018). Furthermore, the second gain is that its inclusive approach which is a resulted from amalgamation of different "views of a large number of enterprises, citizen, and expert survey respondents in industrial and developing countries. It is based on over 30 individual data sources produced by a variety of survey institutes, think tanks, non-governmental organizations, international organizations, and private sector firms."

The Worldwide Governance Indicators of the World Bank reports "aggregate and individual governance indicators for over 200 countries and territories over the period 1996 up to 2017" (The World Bank, 2019). The six dimensions for measurement as indicated includes (1) voice and accountability, (2) political stability and absence of violence, (3) government effectiveness, (4) regulatory quality, (5) the rule of law, and (6) control of corruption. Country level governance if maintained in a good way then it results to sound business environment and leads to a good transparency in the economy of a country. The functions of country level governance as studies indicated are, a promoter of legitimacy, justice, sovereignty of law and market openness. The most important one is that country level governance serves as a regulatory framework that performs fair work, transparency and policies for accountability for a best working environment of business and better economic activities (Avram, Grosanu, &Rachisan, 2015). The literature from previous researches indicated that most of the researches in the field of country level governance are about the importance of its quality they investigated that for sound economic and social developments in a country, practices of country level governance are important and proved more effective (Rachisan, Bota-avram, &Grosanu, 2017).

The governance of a firm and agency theory is inter-related. The agency theory stated that managers of firm with poor governance can easily pursue private benefits but not to those managers of firms with good governance (Gompers et al. 2003; Giroud and Mueller 2011). However, in less competitive industries firm's managers face less competition. By keeping it in view it has been investigated that good governance can lessen agency problems to arise with poor market competition. Analyses form markets of other countries such as U.S market Giroud and

Mueller (2011) suggested that equity returns of firms are observed lower with poor governance practices by the firms and their operating performance is also seemed poor in non-competitive industries. They also investigated that firm‘s value is not good if they have weak governance practices. This is the reason of firm‘s agency problem as it faces a little pressure by product market competition and results in poor governance practices. Previous studies have also determined theoretical based governance mechanism to the efficiency of the firms. As discussed above that agency theory is interconnected with governance, as it shows the relationship between agents and principles.

The shareholders do not have a direct connection with firms but the managers in the firms are acting for their interests. There are more chances in this situation for occurrence of conflicts in managerial firms as the owner and managers when there is separation between all policies and laws.The problem arises at the time of decisions taken by executives (Fama, 1980).However, the top management and executives views the decisions as they are for the more profits of firm and do not control but owned by the firm. The problems created here is when decision and voting power of shareholders are not in their hands. Thus for this reason governance mechanism balances the relationship between shareholders and mangers because agency problem minimizes the productivity of the firms. Furthermore, Baysinger and Butler (1985) further elaborated that the board of directors can effortlessly remove suchclashes from the organization. Executives or board of directors is the backbone of governance and balancing its mechanism as stated byBozec and Dia (2007), Sanchez (2010). They further argue that efficiency of the firm enhances when there is conflict free atmosphere and the executives work properly. The existence of agency problems between executives and shareholders minimizes efficiency and it affects its stock returns.

Country level governance comes at complex debate when it comes to answer the question on different views. The first view about it is, the role of national level governance at the exposure of firm level variables whereas the second one vice versa (Aguilera and Jackson, 2003). The first view in this context says that for having a strong governance mechanism the countries developed some institutions both formal and informal. However, in context of different national governance mechanism, prior studies developed a contextualized view of governance. They developed and explored the antecedents of governance mechanism and explored a theoretical framework on institutional theory. It signifies that governance mechanism in the context of formal and informal results in less significant with organizational context than national context. Further it has been argued that the ratio of new firm‘s entry in an industry is less than that of which the industry grows over the period of time. It results when strategic investments are made by existing firms both in superiority improvement and cost reductions and it ultimately lessen profit gains and encouragements to new entries of firms in industries.

Even though, the firm‘s equilibrium increases when the industry size increases but it is not more than the size of industry growth. However literature revealed that markets with largest sizes there at equilibrium a large number of firms are present. Hence, it has been proved that firms who belong to larger market sizes industries and they observe more competition as compare to those with smaller market size industries. Innovation risks and distress is also raised in results of more competition in an industry as Hou and Robinson’s arguments (2006) firms in low concentration. So, shareholders with larger market size industries demand better returns.

Hence the discoveries of Hou and Robinson (2006) seemed more reliable that industries in with higher concentration earn less returns by firms in account of market, size and momentums. The other results discovered in researches that when firms earn greater returns despite of higher product substitutability as compare to firms with lower product substitutability. However, the second view in this context says that by analyzing firm-level variables the phenomena should be explored, nevertheless the formal and informal features of institutions can be neglected here. Based on this traditions prior researches find agency theory to explain this theoretical framework of governance mechanism. Agency theory in this context is found to explore consequences and antecedents of governance mechanism apart from national environment. Hansmann and Kraakman (2004) supported this view and argued that this develop the idea that the market forces and legal reforms in Anglo-American model, national economies are moving. A lot of formal and informal by following this idea, are becoming similar to US model, that is features by high information transparency, high investor protection, efficient capital markets and a lot or others.

Previous literature explored these two views in a broad way and published articles on country level governance debate. The core issue of country level governance is explored by Van Essen et al(2012)theyin this studies argued that there is a significant and positive impact of firms and country level good governance on firm‘s performance.

They tested their hypothesis by using a sample of large number taken from 36 European countries consisting of 1197 samples. They tested it during the time period of pre and poste financial crises. Their findings suggested that good governance mechanism is much beneficial in every circumstance and in every country. A main contribution of their study is in literature of country level governance is by showing that a good and effective country level governance mechanism can act a contingent for organizational and environmental features. In contrast to this findings also suggested that there are some negative effects of practical implications of governance and control during the period of crises (Van Essen et al, 2012).

Practices of country level governance and financial accounting was conducted by Levine (2002) in US listed commercial banks found a relationship between country level governance and financial accounting. For this study they collected and analyzed data from the time period of 2003-2009 from 315 US listed commercial banks. The interpreted the results that banks show higher level of conditional accounting conservatism when they implement practices of good governance such as they timely report loan losses. These findings opened a gate for debate for a positive role of country level governance practices and refining them. Thus they suggested that governance practices can be complemented by accounting conservatism hence, it improves financial transparency.

Prior researches paid a very little attention for findings of country level governance and its relationship with profitability. However relation of decision making ability at firm’s level and governance at country level making remained under study from last decade. Demirgu ¨c¸-KuntandMaksimovic(2002) examined the macro level governance factors and firm level decision making. However, there is a huge literature existed on the firm level governance featuress, which includes board and ownership structure as one of them. It concluded that firm level governance significantly influence corporate decision. Moreover, the recent studies of Doidge, Karolyi and Stulz (2007) suggested that contribution towards standard governance is because of several of country level governance and that indicates the difference between corporate level governance and firm level governance.

Other researchers about country level governance were also conducted on other variables such as role of R&D on country level governance around the globe. As the domain of research and development is considered non similar to other investments of corporate. However the research and development got 50% expenditures of a firm that is directed for the commissions for the future and upcoming products and services (Hall & Lerner, 2010).

The existing literature on R&D and country level governance show that two important departments of R&D‘s effects on firm‘s market values (Bae& Kim, 2003; Chan, Lakonishok, &Sougiannis, 2001; Chen & Ho, 1997; Doukas& Switzer, 1992; Eberhart, Maxwell, &Siddique, 2004) and the significant factors of R&D spending such as size, cash flow, debt etc; (Lee & Sung, 2005) seemed to reduce both information irregularity in managers and shareholders and moral hazards.

Some of the literature in previous era examined the association between country level governance and R&D. Hence in this regard Beck and Levine (2002) investigated that in countries firms grow faster with strong dependence on external financing and brings higher level of financial development and make more efficient legal systems. The significant influence of country level governance on R&D were also analyzed by the other researchers by examining its influence on the stock markets.

Booth, Junttila, Kallunki, Rahiala, and Sahlstro ¨m (2006) examined that R&D spending influence the stock markets. The relationship between R&D and corporate structure was also investigated by Lee and O‘Neill (2003) in US and Japanese firms. Their findings suggested a positive relation in US firms whereas they found no such relationship in Japanese firms. Bloch (2005) found cash that influential determinants of R&D is cash flow sensitivity which is hypothesized that external funds in the presence of market imperfection may not be a perfect substitute to provide internal funds and give an higher external financing (Hall & Lerner, 2010).

Hence, in this regard R&D provides opaque information and characterized by higher premium and it provide managerial knowledge. Thus for this purpose, good governance is a source of greater disclosure and accountability. Moreover, researches determined that countries having good governance structure strongly facilitate external financing for R&D investment. However there are some confounding factors that are analyzed by prior researchers to affect country level governance.

Examples given in this regard for the countries those have common laws have strongly associated with capital market historically. Furthermore, countries with civil law environment are more concentrated in share holdings and tend to be dominated by banks. It‘s exceptionally difficult to disentangle the interconnection of country level governance with these variables.

The variations of country level governance in studies have found a lot of heterogeneity in governance environment of countries however, this heterogeneity of governance environment would not be eliminated thus the problem related to the confounding factors altogether. For shareholders protection researchers suggested that governance must be enforced. The cost of external finance can be mitigating when law enforced and insider of corporate get information advantage. Study related to law enforcement and country level governance form literature showed that law enforcement is more efficient in improving governance in a country that extensive investor protection. (Defond and Hung, 2004). The law enforcement in countries for better governance show that turnover of chief executives are more likely associated with poor stock returns and inefficient performance when law enforcement is stronger. Thus it is determined that stock prices are inherently more informative in this case. Thus findings suggested that in a strong governance environment capital will be more efficiently allocated. (Durnev, Morck&Yeung, 2004). For sound governance practices there is a global interest on compliance with increasing it. (Ntim et al, 2012).

Prior literature explained after examining public corporations that why these corporations comply and disclose sound governance practices by using a number of theories such as agency theory and resource dependence theory (Samaha et al., 2012). Aguilera & Jackson (2003) argued that governance codes can be explained in the context of neo-institutional theory. However, studies conducted in MENA countries explored that for the pursuing of governance reforms they developed national governance codes. This is more similar to emerging economies thus they adopted a UK style governance code which is “comply or explain” for acquiescence and expose regime (Elghuweel et al., 2017). Apart from this distinct feature it has been stated by authors that MENA countries has unique culture from rest of the world which is mainly highlighted in the form of strong hierarchical social structure, as they give more importance to religious and informal relationships including norms and family loyalty more than formal governance mechanism and accountability. In this regard the most arguably view is whether in this form of culture the standard of governance mechanism is effective or not. governance models previous literature investigated in different national level institutions have differences between Anglo-American” and the “Continental” (Aguilera and Jackson, 2003).

Previous literature on country level governance is subjected to two major limitations. First the researchers widely used impact of governance on profitability in Anglo-Saxon countries and relationship of country governance with equity base pay, security regulators and others. The result found from these studies suggested that practices of some common governance around the globe must be adopted by all firms. But as the matter of concern Shleifer and Vishny (1997) further argued that the firms situated in East Asia and Europe one of the alternative approach of governance namely as direct control form large investors is needed in relational banks.

Second, all of existing governance models is for control of firm‘s power and hence the firm level decisions of governance presented tradeoff in the cost of reduction and the benefit for reduction of cost of capital (Doidge, Karolyi, &Stulz, 2004). Further they argued that in those models the firm controller will improve its governance mechanism in the case in which capital effect is more than offsets the insider‘s loss in private benefits. Researchers conducted on firm level governance investigated that improvement of firm level governance is dependent on string legal protection of shareholders. It is because it provides more support for the enforcement of firm level governance mechanism. However the legal protection in this regard should be clear in most of the cross country variations in firm level governance (Shleifer&Vishny, 1997).

The business enterprises operate for the reason of gaining profits and they shall making profits continually as their major concern is profitability (Akinyomi&Olagunju, 2013). The aim of banks are to generate profits as these are business enterprises. Thus the higher profits of banks indicates their higher performance and their economic success as well. Higher profits are the reasons that firms can attract more and more investors.

Hence, as above it has stated that for good performance firms develop governance mechanisms. Firms with strong country level governance have proved to be more profitable. Previous literature about country level governance and profitability of firms determined that the financial firmness of a firm are determined by the merits of better governance and it make the profitability of firms improve thus a lot more boost in opportunities of organizations come from funds of outside. Furthermore serving government policy goal, lowering vulnerability of the economic disaster, and reducing expenditure incurred in obtaining funds (Latif, Shahid, Haq, Waqas, &Aeshad, 2013). Good governance also encourages support and assurance in the banking system (Mohammed, 2012).

However studies conducted in Sri Lanka, Danoshana and Ravivathani (2013) revealed that there exist a significant connection between country level governance and profitability of organizations. Their study extracted data from different organizations and run regression analysis to check outcomes. The results of their studies explored that the structure of board size and mechanism of organizations have significant effects on profitability along with audit teams.

Data extracted from the cement industry by another research conducted on country level governance in Pakistan showed the relationship between profitability of a company and governance of organization (Cheema& Din, 2013). Panel data covering 15 organizations operating between 2007 and 2011 in the cement sector in Pakistan was used. Relevant information was extracted from financial statements of the selected companies. The research suggested that board size has no considerable association with profitability; meanwhile chief executive officers' duality has effect of organizational profitability.

Moreover, the degree of agreement with the legal structure of countries as developed by corporate and businesses is extensively dependent on good country level governance (Agyemang, Fantini, &Frimpong, 2015). That‘s why a sound structure of country level governance is considered to function as a better moderator of economic interactions amongst several corporations within a business environment (Avram et al., 2015).

Previous studies have been conducted on the relationship between business environment, development and country level governance has discussed this topic widely. (Bota et al. 2018). Researchers investigated that the role of the country in corporation‘ operations are mainly proposes the part of the state as country level governance is becoming an evolving and ultimate method for an economy stated by Stojanovic, Ateljevic, and Stevic (2016).

Thus it has been investigated that corporate environment is highly get effected by country level governance. As previous literature shows that for better public governance the state and anon-state actors along with combined partaking of both civil society and private sector is vital. Furthermore, about business environment as studies determent that it is categorized as a high level of monitoring of rules and laws, it’s effective and efficient control of corruption and an effective level of bureaucracy (Cule& Fulton, 2013). In contrast to this several researchers claimed that there is no such evidence of the impact of good governance on financial performance of a business stated by Al-ahdal et al. (2020).

For better results of country level governance there are two requirements; accountability and transparency (Beck, Demirgüç-Kunt, and Maksimovic, 2006). They are fundamentals for regulations of legitimacy and economic policies for ensuring consistent economic expansion and durable long term development of firm. Moreover in recent era several countries consider it an important factor for economic boom and consider it crucial for business. From the research of a several leading countries indicated that because of poor quality of governance in a country results in failure of economic prosperity mainly, in developing countries (Ngobo&Fouda, 2012).

Throughout the world many studies has been conducted on country level governance that determined a lot of jurisdictions. But a few studies are there that investigated the effect of country level governance on entrepreneurship. The influence of country level governance in prior studies on other variables too including association of country level governance with accounting, auditing and finance (Avram et al., 2015; Hillier, Pindado, Thenmozhi& Narayanan, 2016), other studies shows its relations with economic growth (Bot¸ţa-Avram et al., 2018), FDI (Agyemang, Gbettey, Gatsi, &Acquah, 2019), with ethical behavior of corporations (Agyemang et al., 2015) and investors' protection (Rachisan et al., 2017), entrepreneurship (Grosanu,Bot¸ţa-Avram,Rachis¸an, Vesselinov, &Tiron-Tudor, 2015), expose and compliance (Ernstberger&Grüning, 2013).

Moreover, in the context of banks in Pakistan there is a few literature that determine the association of country level governance and firm's profitability. Kamarudin et al., (2016) explored impact of country level governance on profitability in the framework of banks. In their studies they determined with reference to the capability of banks to produce and maximize financial revenues and confirm its cumulative financial health by examining country level governance of banks and their specific macroeconomics from the implementation of Data envelopment Analysis. Moreover, their studies explained the efficiency of revenue of the conventional banks as well as Islamic banks, the accountability, unimpeded application of law influence and accountability of banks is in a better way if they are operating in Gulf Corporation Council. However, as far as regulatory quality is concerned studies investigated that its impact on revenue efficiency is nil especially in conventional banks however; there exist a significant impact on the Islamic financial institutions. In contrast to this Khan, Al-Jabri, &Saif, (2019) argued that revenue efficiency of traditional banks is significantly affected by the stability of political environment and control of corruption, however in regards to Islamic banks they are not influenced by these factors overall. They further suggested that implementing rules and principles that endorse clearness are required to implement an effective governance mechanism in a country.

Furthermore, prior studies investigated that for examining governance issues in MENA countries accountability of legal system, corporate law and governance structure are crucial issues (Sarhan et al. (2019). This study demonstrates indicators of governance used in worldwide organizations namely as six dimensions;

the six indicators for governance used by worldwide firms namely; voice and accountability, political stability and absence of violence, government effectiveness, regulatory quality, the rule of law and control of corruption and their effect on the ability of banking institutions in Pakistan to generate profits. Both types of banks of Pakistan are focus of this study; including private and public.

Notably, the prediction of profitability is done by the worldwide used indicators moreover the sum of the variables of these indicators interrelated with the perception of a lot of citizens, enterprises and surveys of qualified respondents in developing and developed countries. More than 30 separate data from these aggregated indicators was originated from different sources from the surveys of some school of thoughts, non-government entities, institutions situated in abroad and corporations of private sectors. The current study will demonstrate the profitability of banks through the methods of ROA, ROE and NIM. Thus the research will be classified into three dimensions namely, ROA, ROE and NIM considering them as dependent variables and their functions with governance of an organization. In addition to this as mentioned earlier that the country level governance includes; voice and accountability, political stability and absence of violence, government effectiveness, and regulatory quality, rule of law and control of corruption.

Prior literature demonstrated that the profitability in private banks is better and positive as compare to the public banks as it has been examined that the practices of governance are better performed in private banks as compare to public banks hence the performance is better. Moreover, the results from previous literature demonstrate that there is a significantly negative relation between profitability of Pakistani banks with the measurement of ROA and ROA. However literature revealed that the effects of NIM on the given relation is significantly positive. The current study will be an important body for the policymakers, bankers, regulators academicians and financial analysts. In addition to this researchers found a critical problem of profitability. Moreover they identified problems related to the policy and regulatory solutions. Hence, the current research will demonstrate solutions to the problems related to several regulations and it also introduce policy measures for enhancing the performance as well as profitability of banks. For having better transparency and accountability Almaqtari et al., (2020) suggested that there should be strong rules of laws, greater regulatory quality, judicial enforcement and significant force of corruption must be encouraged.

Henceforth, for the stakeholders it is inclusive to develop a framework of practical policy for reconsidering the country level governance dimensions so that poor governance practices can be avoided and also low profitability can be avoided. Furthermore Base III implementations has been noticed to be implemented strictly and efficiently. In this regard the current research will make a unique contribution which will also be significant for the contemporary literature from country level governance of profitability of banks. The previously documented literature highlighted the importance of country level governance and its dimensions and considered it a very important factor for determining of a better performance of finances in banks and their environment as well (Almaqtari et al. 2020). As concluded by Byun et al. (2012) that firms operating in a noncompetitive industry with best practices of governance enhances more firm importance.

Sharpe (1964) has formulated basic portfolio analysis model. Sharp has extended the work of Markowitz (1952) that stocks are expected to go with the flow of market, he has presented model for computing expected systematic risk. He linked market securities with several other factors. The model of Sharpe believes that the returns of securities are linearly correlated to the variations in the market wide index, by a well-known level of sensitivity; in addition to this he investigated that, returns of securities are made with an already known mean and variance by the firm‘s performance. Most important assumption of Markowitz model concerning is the behavior of investors. They proved that investors prefer higher returns for a specified level of risk for their stocks and in the same way less risk for specified range of expected returns. Studies conducted in other countries by Black, Jensen and Scholes (1972) have examined the equity returns of New York stock exchange from the period 1926 to 1966, they examined it through relaxing number of assumptions in the traditional CAPM (as explained in introduction). Their study finds efficient measure for mean of betas of the portfolios after making groups on the basis of beta and via dividing portfolio on the betas foundation, by eliminating several biases for instance measurement and selection bias. In addition to this further studies of Pastor and Stambaugh (2000)have determined that various investors' portfolio preference who modernizes the previous beliefs of them on the basis of asset pricing model of optimal portfolios in stock returns. Though, the asset pricing model transformed significantly and with the modern approaches though these differences are eliminated.

In addition to this, for promoting a fair regulatory framework, justice, legitimacy and market openness a good country level governance is crucial that points to better and comprehensive economic activates, transparency in the economy and sound business environment. (Avram, Grosanu&Rachisan, 2015).

Moreover, the legal structure of the country is dependent on the governance of its country. The good governance practices leads to good performance of enterprises and businesses (Agyemang et al., 2015). Beck, Demirgüç-Kunt, Laeven, et al. (2006) elaborated it further that there are necessary requirements for good country level governance those include accountability and transparency.

Prior researchers studied firm's performance and investigated its relationship with corporate performance and country level governance in different countries. Studies conductedin the US determined the influence of firm's performance and board structure. Most of studies were conducted on developed countries and ignored the problem of performance in under developed countries (Caprio et al., 2007).

Different studies have been conducted to the profitability in banks and its impact of bank-specific (internal determinants) and macro-economic (external determinants) on in some of under developed countries such as in India (Al-Homaidi et al., 2018; Almaqtari et al., 2018; Bapat, 2017; Maiti& Jana, 2017; Almaqtari, Farhan, Thabit, & Al Homaidi, 2020; -Homaidi, Almaqtari, Yahya, &Khaled, 2020).

Previous studies have also determined theoretical based governance mechanism to the efficiency of the firms. As discussed above that agency theory is interconnected with governance, as it shows the relationship between agents and principles. The shareholders do not have a direct connection with firms but the managers in the firms are acting for their intersts. There are more chances in this situation for occurrence of conflicts in managerial firms as the owner and managers when there is separation between all policies and laws. The problem arises at the time of decisions taken by executives. (Fama, 1980). However, the top management and executives views the decisions as they are for the more profits of firm and do not control but owned by the firm. The problems created here is when decision and voting power of shareholders are not in their hands.

The way in which an organization is administered, directed or controlled is referred to as governance. This term includescertain set of rules and regulations that contribute to the system in which current and potential stakeholders are perceived by the company along with it governance also affects the manager‘s decision. The rights and duties of board of directors, managers, shareholders and all stakeholders are specified by coporate governance in a firm. It specifies the rules and procedures and alsoprovides certain assistance in decision making assistance on important corporate affairs. The concept of governance for corporation is a structure base as it offers the structure through which a firm ‘s goals are defined and set, along with it, it also provide means of getting those objectives. governance defined the ways to monitor the performance. Firms are meant to work for the benefits of its stakeholders so as far as governance is concerned the firm with governance can bring into line the interests of managers and its investors so both get benefits without conflicts. governance make capital of the firm effectively occupied and mobilizes efficient use of resources in larger economies and within the companies.

Nevertheless influence of product market competition on stock returns would be positive or negative across market and different countries. Studies conducted in the markets of U.S by Hou and Robinson (2006) determined the fewer industries with concentrated firms face higher market competition and get less returns. Because the firms that face rigid market competition are seemed to be involve in innovation and their outcomes are steadier with creative- destruction theory. However examinations of association between market competition and stock returns in Korean markets showed some of unique characteristics. Traditionally, the growth of Korean economy is the outcomes of intervention, planning and support of controlling government and the government has provided to large corporations with several subsidies to help them in competing foreign counterparts. That‘s why Korean economy has developed quickly as the subsidies and firm friendly policies are in their favor. However in the period of chaebol firm‘s development which was formed by a family with a unique business group of people Kang 1997; Kim 1997; Steer et al. 1989) and they included companies named as Samsung, Hyndai, LG, Doosan and GS, they formed a conglomerate comprising of 61 business and heir total value is approximately 2258 trillion according to Korean won. (Korea fair trade commission press release, 1 April 2015).

Resultantly if the idea is being accepted that product market competition is being affected by stock returns then other scopes of product market competition are also needed to be investigated and how they are related with stock returns. Previous studies as was conducted in Pakistan investigated the relationship between stock returns, product substitutability and size of market and industry concentration. However the relationship between product substitutability and market size with stock returns has been explored previously.

As stated earlier that when a firm‘s products are easily substituted by other firms then it seemed that these firms possess diminished pricing power in product markets. So it would be difficult for a firm to pass on any cost shock to its consumers. Therefore, under these considerations it can be argued that the cashflows for such a firm will be more volatile than those for industries whose products can't be interchangeable.

Hence, with reference to these consequences it can be claimed that stockholders will demand advanced stock returns in the dimension of product market product substitutability. The relationship between the second dimension market sizes of product market competition and stock returns also has been investigated and are argued that more firms are seemed to enter in industry if the size of market enhances in an industry, attacked by the scene of higher profitability. Consequently, it leads to a price competition (Sutton 1991; Mas-Colell et al. 1995).

Further it has been argued that the ratio of new firm‘s entry in an industry is less than that of which the industry grows over the period of time. It results when strategic investments are made by existing firms both in superiorityimprovement and cost reductions and it ultimately lessen profit gains and encouragements to new entries of firms in industries.

Thus for this reason governance mechanism balances the relationship between shareholders and mangers because agency problem minimizes the productivity of the firms. Furthermore, Baysinger and Butler (1985) further elaborated that the board of directors can effortlessly remove such clashes from the organization.

Executives or board of directors is the backbone of governance and balancing its mechanism as stated byBozec and Dia (2007), Sanchez (2010).

Prior literature of Cheng, Gutierrez, Mahajan (2007), investigated that in unchallenged competitive situations banking systems can operate. However there was observed lower completive during the Europe level banking system as compare to the United States banking system. Moreover it was observed that it sustain in being an additional competitive as compare to small level banks. For the higher range of world economies Clerides (2014) created certain use of indicators such as Lerner and Bone for evaluations, later researchers investigated the Lerner indices in various countries world wide. Prices were observed to be higher in the market concentration and it was linked with greater prices in compare to normal profitability. Ho and Saundres (1981) observed the requirement of deposit in banking system and loan supplies. However, in relation to this estimation the interest rates of banking systems were estimated to be dependent on four factors:

- The bank‘s management risk aversion‘s degree
- Industry‘s market system
- The transaction policy size of the banking system
- The interest system‘s variance

The influence on the flows has been observed by the several scholars by the limitations and supervisions of various banking systems. In their views the opportunity cost and the chances of loan envisions the mandatory assets in more of the factors that highly effects the spread flows including inclusions not remained part of this model as it is under study. In concentration market maintaining the higher profits could be the results of moiré and more creative efficiency. The hypothetical analysis of efficiency states that a diverse relation between efficiency and competition has been studies and in results by reversing the casualty flows from efficiency to comparison in the scenario of exchange commission.

The study of Berger (1995) suggested that the relation of hypothetical as a prove of efficiency in United states banking systems has a hold. However in contrast to this in European banking systems there appears a structural determinants as an additional significance but the SCP theories comes as a hold of these type of studies. The determinants other than the concentration of markets and systems as suggested by the non-structure techniques may have some influence on competitive attitudes. These includes entry and exist barriers and the market section‘s main contestability. Hence, later some of other techniques were established in the literature of new industrial organization. Other researchers also added that the minimization of cyclical fluctuations by the banking systems of profitability by the transfer of total revenues among non-interest income has been depended less on the environment of business. The study of Meslier, Tanceng & Tarazi (2014) it has estimated that in the financial markets the higher competition leads banks to higher diversity.

However, majority of the prior studies investigated profitability by applying Return on Asset (ROA) and Return on Equity (ROE) for the purpose of measuring of bank‘s profitability. The measurement of ROA is through the ratio of net profit from subtracting the tax and then dividing it by all the assets (Ozili&Uadiale, 2017; Tiberiu, 2015; Yeon& Kim, 2013) hence, the calculations of ROE is from the ratio of net profit from subtracting the tax from shareholders equity scale (Eljelly&Elobeed, Eljelly&AbdelgadirElobeed, 2013; Jedidia, 2016; Kythreotis, 2014). In contrast to this there are a few studies that investigated bank‘s profitability using Net Interest Margin (NIM) in under developed countries. Bapat (2017) stated that through risk and corporate diversification banks can potentially enhance their revenues no matter the NIM pressure of banking sector remains there. The results of NIM is extracted from the division of the net interest income with the aggregate assets (Saif, 2014; Yeon & Kim, 2013). Furthermore the Capital to risk weighted asset ratio (CRAR) operated for the landscape of whole banks and fulfill the Basel III‘s requirement at minimum level. Studies demonstrated that the net interest income of banks is depleted by the total operating expenses. Almaqtari et al., (2020) suggested that for the bank‘s long term sustainability the potential stress of financial is not distinguishable. The financial performance of an organization depicts that financial resources of organization has been used properly and how fit and healthy the financial situation of the organization is. Practices of governance monitor accountability of the Board of directors and its managers it also enhances confidence of international investors and board of directors of the firm and assist lower cost investment capital. The legal compliance is ensured by Board of directors of the firm it also ensures to make fair decisions which are better for the firm. So, it is determined that governance practices make it difficult for corrupt practices if any to not take cause however it might not exterminate them immediately.

Researchers have studies effect of governance on several variables in different countries. As Gompers et al. (2003) examined the effect of governance on equity prices in stock market U.S firms and determined that firms showed higher stock market performance when they exhibit good governance as compare to firms with no exhibition of governance. They explain it through relationship of governance, corporate cash flows and stock returns to investigate that in efficient market stock returns is highly affected by governance. Theyfurther argued that to prevent managers from diverting resources and impedes their efforts for value creation of firm its necessary to have better governance in the roots. It also results not only to change the likely cash flow but along with it the risk-return trade-off stock investors. However difference in stock reruns of better and poorly governed firms is investigated by Core et al. (2006) is insignificant in Korean markets. Other researchers argued that the correlation amid governance and stock returns are explained by investor learning effects from these results that after the investors come to know that how important is the governance for the firm then the abnormal stock returns of firm even with food governance decreases. (Bebchuk et al., 2013). With regards to industry concentration the listed firms in Korean stock market showed that quality of governance has significantly negative association with stock returns among firms with highly competitive industries. As Pakistan is also among one of the emerging markets hence it can be argued that similar results can be observed. Byun et al. (2012) investigated that in non-competitive industries firm's value increases when it operates good governance. Moreover, the effects of substitution between among governance and market competition are statistically insignificant and their impact on firm's stock returns are also less significant in less concentrated industries. Despite this there are findingsthose in greater competitive industries when firms practice good coporate governance practices is more in association with lower returns on stocks as comape to firms in highly competitive industries(Ryu et al. 2015).

Contrast results of governance and stock returns in other countries have been found. The studies that were conducted other than U.S firms documented that firms have higher retrns in stock markets when their governance practices are poor. The studies conducted in Japanese market theAman and Nguyen (2008) investigated that in Japan firms with poor governance are outperformed in market by the firms with better governance practices. They documented the reason for this is their higher market exposure. Moreover, analysis from Asian market such as China, Hong Kong, India, Taiwan, Thailand and Koreait was determined that betas, expected returns and realized earnings of poorly governed firms are higher than the firms who has good governance portfolios. (Kouwenberg et al., 2014). That's‘ why the relationship of quality of good governance and stock returns is different amongst the U.S and evolving markets.

This is further claimed by Bebchuk et al. (2013) that in emerging markets its still have to materialize that what are the effects of investor‘s learning.Researches in Korean market about noise traders report that individual traders mainly who are without difficulty get affected from short term profit pursuing purposes, behavioral biases and investor sentiment play an important role in Korean financial market. (Chung et al. 2016; Webb et al. 2016; Yang et al. 2017).On the other hand, the characteristics of market-specific investors are further leadings to differences in stock market behavior and its comebacks to the better governance. However as compare to Pakistani stock market, the investors in Korean market have this perception that the response of markets to governance is interpreted and that is significant in its costs and risks. However, in the case of other emerging countries it has been observed that practices for maintaining good governance are not considered important as investors don't see it beneficial and consider it a financial burden for the firm hence it is reported by several researchers by aligning its similarity with Pakistan that better governance is negatively correlated with firm‘s stock returns.(Ryu et al. 2011).

To analyze the relationship among governance and its effects on stock returns-Gompers et al. (2003) pioneered this holistic approach. They on based on their investigation constructed the Governance Index that‘s also called GIM Index. It employed on 24 provisions to limit or protect shareholders rights. GIM Index has scores and from those scores a group under Dictatorship portfolio includes firms with weak shareholder protection but the democracy portfolio is under the right shareholders of firms. On base of this the results of their studiesit has been investigated that statistical significance of Dictatorship portfolio is outperformed by democracy portfolio. Furthermore, the outperformance of the Democracy portfolio drops the statistical significance when the sample period is divided into two that indicates that with good governance it can be expected good returns and that can be non-linear. However, recent studies asstirred via q-theory (Cochrane, 1991), Hou, Xue, and Zhang (2015) on stock returns presented a two period general equilibrium model and determined that the profit maximization of a firm in first order condition proved a positive relation between expected returns and profitability. In addition to this the empirical analysis of Wang and Yu (2013) investigated that the gross profitability premium could be caused by common mispricing components rather than compensation for risk. In this situation, researches were attempted to propose a source of risk associated with gross profitability that is particularly product market competition. Hence, Generally, firms' expected cash flows are affected by their operation decisions, which are determined by strategic interactions among product market participants.

If firms' expected cash flows are rationally priced in the financial markets, the market price of expected cash flows would reflect the structure of product markets and it can affect stock returns overall. Therefore, the cross-sectional pricing impacts of gross profitability, which is a better accounting proxy for future expected profitability, should be affected by product market competition. So far, studies make it confirm that expected returns on expected profitability are greater in competitive industries. Then, it is natural to ask the source of driving force of a pricing kernal since equilibrium asset price is expressed as the expected product of a pricing kernel and the cash flows from the asset. So studies also concluded that the risky innovation as a potential determinant of a pricing kernel on expected profitability. According to Schumpeter (1912), corporate profits arise from entrepreneurial innovation and such innovations are more likely to occur in competitive industries and hence it highly affects stock returns. Thus, firms in competitive industries are more likely to be engaged in innovation to maintain their profitability and competitiveness as it results in higher stock returns but firs usually don‘t go for it as innovation is generally a risky operating process. In the real options model developed by Berk, Green, and Naik (2004), R&D investments are a series of compound options on the systematic component of risk associated with cash flows and these R&D ventures demand a higher risk top than lower cash flows, because the risk of options is higher than that of underlying assets.

For improving good financial performance of firms and to reduce the investor‘s risk good governance practices are essential to regulate (Wakaisuka-isingoma et al., 2016). Prior studies investigated that it good country level governance significantly influence profitability of firms. Prior researchers also studied impact of Country-level governance on entrepreneurship in different states over the period of 2007 to 2012.

Groşanu et al. (2015) studied country level governance by using World Banks's six metrics and determine its impact on the business climate. The study investigated that political stability, regulatory efficiency and entrepreneurship impact the market climate. Henceforth good country level governance plays a vital role in economic growth (Ribeiro-Soriano & Galindo- Martín, 2012). In addition to this Chambers and Munemo(2017) argued that financial performance of a firm is highly determined by country‘s regulatory and institutional environment. Further, they report that lack of high-quality institutions (regulation quality, voice and accountability, and political stability) has a significant effect on profitability of banks.

2.2 Hypothesis

H1: Country level governance has positive and significant effects on Banks performance.
H2: There is a positive and significant effects of deposits on banks profitability.
H3: There is a positive and significant effect of capital on banks profitability.
H4: There is a positive and significant effect of loans on banks profitability.

H5: There is a positive and significant effect of size on banks profitability.

Chapter 3

Data Description & Research Methodology

The data description and methodology which were used in this study and explain the different method and test used for this study and analyzes population, sample, and source of data which includes for this analysis. The main theme of this chapter shows about data collection mechanism from which sources are used to collect data. The data is collected from the Pakistani Banks. To find the impact of country level governance on banks performance.

3.1 Population

Population of the study comprises all banks working in Pakistan.

3.2 Sample Size

The representation of population is done be the sample size. Sample size includes data of those banks which gives the complete information regarding to this study. Study included dataset comprises are 38 banks of Pakistan from the year 2006 to 2019. Sample size of the study 38 commercial banks of Pakistan.

3.3 Sources of the Data

This study is being conducted on the basis of secondary data which is already ready and available on different websites, financial reports. For the collection of data of variables this study includes different sources. The data of control variables and dependent variable is taken from annual financial reports of the banks and SBP published FSA (financial statement analysis). For the independent variable CGI the data were collect from the website of country level governance.

Table 3.1: Sample of banks

S.NO	Name of Banks	S.NO	Name of Banks
1	Allied Bank Limited	20	Industrial development bank of Pakistan
2	AL Baraka Bank (Pakistan)ltd	21	JS Bank Limited
3	Askari Bank Limited	22	KASB Bank Limited
4	Bank Al-Habib Limited	23	MCB (Muslim commercial Bank) ltd
5	Bank of Punjab	24	Meezan Bank Limited
6	Bank of Khyber	25	National Bank of Pakistan
7	Bank Al Falah ltd	26	NIB bank Limited
8	Bank Islamic Pakistan Limited.	27	Oman International Bank
9	Barclays Bank PLC	28	Punjab provincial cooperative Bank limited
10	Citi Bank ltd	29	Samba Bank Ltd
11	Dubai Islamic Bank limited	30	Sindh Bank Limited
12	Duetsche Bank Limited	31	Silk Bank Limited
13	Faysal Bank Limited	32	SME Bank Limited
14	First woman Bank Limited	33	Soneri Bank Ltd
15	First Dawood Islamic bank	34	Standard Chartered Bank
16	Habib Bank Limited	35	Summit Bank limited
17	Habib Metropolitan Bank Limited	36	The Bank of Tokyo Mitsubishi UFG ltd
18	HSBC Middle East Limited	37	UBL (United Bank)ltd
19	Industrial And Commercial Bank of chiana	38	Zarai Tarkiyati Bank Limited

3.4 Descriptive Statistics

Statistical behavior of data is captured by using the descriptive statistics. Descriptive statistics sum-up or elaborate the traits of data set. A data set is a combination of responses from population or sample. There are two main types of descriptive statistics central tendency and variability. Descriptive statistics includes mean which provide the average of data, median which divide the data set into two equal segments and it is the mid value of data set, standard deviation provides the information that how much the difference of data from its mean value. Mean and standard deviation must be used together if used separately both will be meaningless. Positive and negative spread of data captured by using the skewness and kurtosis infers about the flatness of data spread. By using the descriptive statistics, we capture the acute infers of variables.

3.5 Correlation Analysis

The degree of strength among variables is determined by correlation analysis. Correlation analysis is a very helpful tool for determining the direction of relationship among research variables. It tells directions by indicating positive and negative relationship among different variables. The range of correlation among variables lies from -1 to +1. If between two variables the correlation results are low then it shows that there are low chances of multicollinearity on the other hand if results between two variables show high correlation, then there are high chances of multicollinearity.

3.6 Econometric Model

In this study Panel data is used to capture the influence of CGI on overall Pakistani banking sector. Estimation of panel data is usually done by POLS, fixed and random effect model.

3.6.1 Panel Data

Panel data is the mixture of both type of data time series and cross-section data.

This study contains both type of data. A balanced panel is the outcome when time observation and cross section have same series in a panel. However, Gujarati, (2003) stated that the panel is unbalance panel when there is a difference between series of time observation and cross section panel.

In present study, mainly the model can be written as follows:

$$ROA_{it} = \beta_0 + \beta_1 GI_t + \beta_2 size_{it} + \beta_3 capital_{it} + \beta_4 loans_{it} + \beta_5 deposits_{it} + \epsilon_{it} \quad (3.1)$$

$$NIM_{it} = \beta_0 + \beta_1 GI_t + \beta_2 size_{it} + \beta_3 capital_{it} + \beta_4 loans_{it} + \beta_5 deposits_{it} + \epsilon_{it} \quad (3.2)$$

$$ROE_{it} = \beta_0 + \beta_1 GI_t + \beta_2 size_{it} + \beta_3 capital_{it} + \beta_4 loans_{it} + \beta_5 deposits_{it} + \epsilon_{it} \quad (3.3)$$

3.6.2 Model

3.6.2.1 Common Constant Model

The first model of common coefficient model. It has constant intercept across all cross sections and time period.

$$Y_{it} = \alpha_0 + \beta X_{it} + \varepsilon_{it} \quad (3.4)$$

Where:
Y, representing the dependent variable
X, representing thelist of independent variables
ε , representing the error term

3.6.3 Fixed Effect

In this method the constant values are treated as group section specific. It indicates that this model, for each group, implies different constants. The fixed effects model is also called as the least-squares dummy variables model because in order to allow for different constants for each group, it includes a dummy variable for each group.

FEM particularly captures all effects which do not vary over time and also which are specific to a particular individual.

$$Y_{it} = \alpha_1 + \beta_1 X_{1it} \beta_2 X_{2it} + \ldots\ldots \beta_k X_{kit} + \varepsilon_{it} \tag{3.5}$$

In this case the regression equations will be as follows,

$$\begin{aligned}
ROA_{it} &= \beta_0 + \beta_1 GI_t + \beta_2 size_{it} + \beta_3 capital_{it} + \beta_4 loans_{it} + \beta_5 deposits_{it} + \epsilon_{it} \\
NIM_{it} &= \beta_0 + \beta_1 GI_t + \beta_2 size_{it} + \beta_3 capital_{it} + \beta_4 loans_{it} + \beta_5 deposits_{it} + \epsilon_{it} \\
ROE_{it} &= \beta_0 + \beta_1 GI_t + \beta_2 size_{it} + \beta_3 capital_{it} + \beta_4 loans_{it} + \beta_5 deposits_{it} + \epsilon_{it}
\end{aligned} \tag{3.6}$$

3.6.3.1 Redundant Fixed effect or F Test

This test helps the decision maker to take decision between Common constant model and fixed effect model. The decision is taken on the basis of F stat. and Chi-square. if F stat. and Chi-square cross-section is below than 0.05 so fixed effect model will apply if P-value is insignificant than common constant method will be used.

3.6.3.2 Random Effect Model

For estimating a model there is an alternative model too, that is the random effect model. The particular distinction between the fixed effects and the random effects method is that the handling of constants is as random parameter not as fixed for each section. Henceforth the variability of the constant for each section comes from the fact that:

$$\alpha_i = \alpha + \nu_i$$

where ν_i is a zero mean standard random variable

As compare to fixed effect model Random effect model some of parameters for estimation. However, it provides the permission for further independent variables with same number of observations.

Where ν_i is a zero mean standard random variable

The random effects model therefore takes the following form:

$$Y_{it} = (\alpha + \nu_i) + \beta_1 X_{1it} \beta_2 X_{2it} + \ldots\ldots \beta_k X_{kit} + \varepsilon_{it} \tag{3.7}$$

Where,

Y= is dependent variable performance (TOBINS Q).

X= is the list of independent variables (economic policy uncertainty,).

X (k)= explanatory variables

i =represent different banks

t= shows the Time

ε= represent error term.

3.6.3.3 Huasman Test

Huasman test implies when there is a need to take decisions between random and fixed effect model. When the F stat. and Chi-square of cross-section is lower than 0.05 than fixed effect model is used but when P-value is insignificant then common random effect model is considered to apply.

3.7 Description of Variable

This study employs number of variables including ROA, ROE, NIM measures and control variables. Control variables include bank specific variables such as capital, size, loan and deposits.

The description and measurement of the variables is discussed below.

3.7.1 Return on Asset (ROA)

Return on asset is measure of profitability variable. It is calculated by dividing the net income of the company by its total resources of assets. Net income is calculated by deducting the company's taxes for the year.

Financial institution is more interested in the firms which have higher return on assets or profitability, because profitable companies have more returns, their stocks are traded more frequently and consequently have higher trading volume.

3.7.2 Return of Equity (ROE)

ROE is measured by net income before tax by dividing total shareholder equity

$$\text{ROE= net income/ shareholder equity}$$

3.7.3 Net Interest Margin (NIM)

NIM is measured by Net interest income divide by total assets

$$\text{NIM = net interest income/ total assets}$$

3.7.4 Country Level Governance

Six country level governance indicators was also developed by The World Bank and their use is most common in academics as narrated by Bota-Avram et al.,(2018).These worldwide indicators as narrated in World Bank reports as The Word Wide Governance Indicators (WGIs)"aggregate and individual governance indicators for over 200 cointries and territories,

3.7.4.1 Six dimensions of the Worldwide Governance Indicators

1. **Voice & accountability:** Reflects perceptions of the extent to which a country's citizens are able to participate in selecting their government, as well as freedom of expression, freedom of association, and a free media.
2. **Political stability no violence:** perceptions of the likelihood of political instability and/or politically-motivated violence, including terrorism.

3. **Effectiveness of Government:** The quality of public services of the firm depicts its degree of independence and its civil services form the pressure of politics. However, the implementation and formulation of policy and commitment of government for such policies and their incredibility.

4. **Regulatory quality:** The regularity quality of the firm depicts its capacity to formulate and monitor strong policies and regulations that enhance and permit the development of private sector.

5. **Rule of law:** it mainly exhibit the perception on which the agents get confidence and abide the societal rules but apart from this the other factors include quality of contract enforcement, police and courts and some of the crimes and violence.

6. **Control of corruption:** The power of public in here is exercised for the benefits of a person that mainly include corruption types and capture of elite and private interests of state.

3.8 Control Variables

Deposits:(Dep)

Deposits are the money that has been put into one bank or all the banks by the depositors. Deposits of the bank are calculated total deposits of the bank divided by total assets.

Formula: deposits = total deposits/ total assets

Capital:(Cap)

Capital is calculated by shareholder equity (share capital, reserve, Unappropriated profit) divided by its total assets. (Fang et al. 2014; Niu2016)

Where,

Capital = shareholder equity/ total assets

Size: (Sz)

Size of the bank is most effective control variable. Many types of bank size such as large, medium and small. In this study, size is measured through proxy its assets by taking the Natural logarithm of total assets of the bank.(Fang et al.2014;Niu,2016)

Loans:(Ln)

Loan is the money that a bank lends to a particular customers like businesses, investor, households. Banks loan is measured through total loans and leases divided by total assets.

TOTAL LOAN AND LEASES/ TOTAL ASSETS

Chapter 4

Results and Discussion

4.1 Descriptive Statistic

Table 4.1 explains behavior of data about all variables of the research model from the period of 2006 to 2019. Data behavior was studied to explore its accuracy before performing other statistical tests. Descriptive statistics shows that general behavior of the data, including the dependent, independent and control variables.

The descriptiveTable 4.1 is showing the descriptive statistics of all variable which are used in this study, the mean value of ROA is 0.0052 it means that banking sector of Pakistan performs 0.05% in a year. And its standard deviation is 0.014. ROA is used as proxy for performance of a bank. The maximum and minimum are 0.053 and -0.076. The Skewness is -1.4818 means that data is negatively skewed and Value of Kurtosis is 6.800. As value of kurtosis is above from 3 so we can say that the data is peaked. The mean value of ROE is 0.021 which show .21% Return on equity in a year. ROE is used as proxy for bank performance, and its standard deviation is 0.876. Its maximum and minimum are 2.347100 and -14.74. The Skewness is -14.7 means that data is negatively skewed and value of kurtosis is above than 3 so we can say that the data is peaked. The mean value of net interest margin is 0.76% and maximum and minimum of 0.120900and 0.000200or its standard deviation is 0.019417. Data is negatively skewed and Value of Kurtosis is 5.483. The mean value of capital is 0.1489with maximum and minimum of 0.788and -0.0310. Average of capital is observed as 0.139 while data is found positively skewed. Value of Kurtosis is 8.7041, which means data is peaked.

The mean of loans is 0.482 which means average .482% loans worth having the commercial banks of the Pakistan with the maximum and minimum value of 0.59 and 0.40. Its standard deviation is 0.047. The Skewness is 0.153 means that data is positively skewed and value of Kurtosis is 2.82, which means data is marginally flat and data is not normally distributed. The mean value of deposits is 0.668, this indicate the average deposits having commercial banks is 0.668% every year with maximum and minimum value of 0.0284 and 0.908. Average deposits are observed as 0.208while data is found negatively skewed. Value of Kurtosis is 4.56154 which mean data is peaked.

The mean of size is 18.42, its mean that average 18.42% total assets having by the commercial banks of Pakistan with maximum and minimum 21.520 and 15.05150. There is some little bit difference between bank size values and its standard deviation is 1.4777 while data is negatively skewed and Value of Kurtosis is 2.250. Value of kurtosis is less than 3 which indicate that the data is flat. (How to write GI)

Table 4.1: Descriptive Statistic

	ROA	**ROE**	**NIM**	**CAP**	**LOANS**	**DEP**	**SZ**	**GI**
Mean	0.0052	0.0218	0.0765	0.1489	0.4604	0.6688	18.424	-1.0907
Median	0.0080	0.0793	0.0784	0.0994	0.4772	0.7435	18.438	-1.1106
Maximum	0.0530	2.3471	0.1209	0.7880	0.7864	0.9085	21.520	-1.0118
Minimum	-0.0764	-14.742	0.0002	-0.031	0.0026	0.0284	15.0515	-1.1782
Std. Dev.	0.0186	0.8769	0.0194	0.1391	0.1395	0.2080	1.4777	0.0593
Skewness	-1.4818	-14.731	-1.2185	2.2843	-0.5737	-1.5749	-0.1681	0.0959
Kurtosis	6.8003	248.61	5.4833	8.7041	3.5006	4.5615	2.2507	1.5328

4.2 Correlation Analysis

Table 4.2 explains the relationship among independent and dependent variables. Pearson correlation test is used to measure the direction and strength of the relationship among variables the value of correlation coefficient ranges from positive 1 to negative 1. if the value of correlation coefficient is equal to 1 then its mean that there is perfect relationship among the variables. When the value is zero then it shows that there is no relationship among variables. The coefficient sign provides the direction and relationship of variables.

Findings of correlation indicate the insignificant positive relationship of ROA with ROE, NIM, GI and size while significant positive relationship with loans, deposits, and capital is negative insignificantly associated with ROA. On the other hand, ROE have positive significant association with NIM and loan. ROE have significant positive association with deposits, capital while size and GI have positive insignificant relationship with ROE. However, NIM is insignificantly and positively associated loans, deposits and size. On the other hand, NIM negatively insignificantly associated with capital and GI. Findings of capital show negative insignificant relationship with loans, deposits, size and GI. On the other hand, deposits and size positively and insignificantly while GI is negatively significantly associated with loans. Moreover, deposits have insignificant positive relationship on the other hand, GI positively significantly associated with deposits. Further, size has insignificantly positively associated with GI.

Table 4.2: Correlation Analysis

	ROA	**ROE**	**NIM**	**CAP**	**LOANS**	**DEP**	**SZ**	**GI**
ROA	1							
ROE	0.3374	1						
NIM	0.1557	-0.0319	1					
CAP	-0.1965	0.0161	-0.5133	1				
LOANS	0.0535	-0.0551	0.4768	-0.4016	1			
DEP	0.0017	0.0081	0.3573	-0.6850	0.1732	1		
SZ	0.3705	0.1163	0.3547	-0.6570	0.2870	0.5174	1	
GI	0.1472	0.0869	-0.3219	-0.0723	-0.0458	0.0372	0.1036	1

4.3 Model Specification

Table 4.3: ARedundant Fixed Effects Tests

Effects Test	**Statistic**	**d.f.**	**Prob.**
Cross-section F	7.095329	-39,283	0
Cross-section Chi-square	223.69137	39	0

The decision is taken on the basis of F stat. and Chi-square. IF Chi-square and F stat. is below from (0.05) so that fixed effect model will be used or common coefficient method will be used if P-value is insignificant which is higher from (0.05). Table 4.3 in this study the p-value is significant (0.000) however, the fixed effect model should be used.

TABLE 4.4: Correlated Random Effects - Hausman Test

Test Summary	**Chi-Sq. Statistic**	**Chi-Sq. d.f.**	**Prob.**
Cross-section random	18.4425	5	0.0024

Hausman test implies when there is a need to take decisions between random and fixed effect model. When the F stat. and Chi-square of cross-section is lower than 0.05 than fixed effect model is used but when P-value is insignificant then common random effect model is considered to apply. Table 4.4 shows the P value is significant than the fixed effect model is used.

4.3.1 Fixed Effect Model: Impact of GI on NIM

TABLE 4.5: Impact of GI on NIM

Variable	**Coefficient**	**Std. Error**	**t-Statistic**	**Prob.**
C	-0.2726	0.0334	-8.1511	0.0000
GI	0.0104	0.0145	0.7229	0.4708
CAP	0.0276	0.0113	2.4353	0.0155
LOANS	0.0454	0.0085	5.3327	0.0000
DEP	0.0457	0.0104	4.3901	0.0000
SZ	0.0086	0.0015	5.6095	0.0000
Effects Specification Cross-section fixed (dummy variables)				
R-squared	0.7244		Mean dependent var	0.0765
Adjusted R-squared	0.6814		S.D. dependent var	0.0194
S.E. of regression	0.0109		Akaike info criterion	-6.0648
Sum squared resid	0.0338		Schwarz criterion	-5.5432
Log likelihood	1036.5910		Hannan-Quinn criter.	-5.8567
F-statistic	16.8474		Durbin-Watson stat	1.9870
Prob(F-statistic)	0.0000			

The Results of table 4.5 shows that the country level governance negatively affects the bank performance. This table shows the effect of GI on NIM. NIM is used as a proxy of bank performance. Random and fixed effect model is used to elaborate the impact of independent variables on bank performance. The p-value of GI is (0.4708) which is more than from (0.05) and coefficient value is (0.010437). It means that GI positively and insignificantly effect on bank performance. Some bank specific variables are included in this regression equation. Loans have positive coefficient (0.045391) and p-value is (0.000) which is less than from (0.05). It means that when banks advance loans it will positively affect the bank performance. The

capital of banks has significant p-value (0.0014) with its coefficient value (0.0276). It means that when banks have higher capital it will positively and significantly affect bank performance which means high capital leads to higher NIM. The p-value of deposits is (0.0000) which is less than from (0.05) and coefficient value is (0.045744). This result show that when banks have more deposits it will positively and significantly affect the bank performance. Deposits are the one of main earning sources for banks. The size of banks has significant p-value (0.0000) with its coefficient value (0.008579). It means that when banks have larger size it will positively and significantly affect bank performance. The bank size is the always discussing point in the banking sector. It indicates that more assets positively affect the bank performance. Moreover, the R-squared value builds a suitable

source for the model of country level governance and bank performance. In next section banks data set results shows that value of R2 (0.724418) which mean that dependent variable bank performance only 35% influenced through these independent variables country level governance. Adjusted R-square value is (0.681419). Explanatory power of model is low which is usually on lower side in these types of studies. F-statistics talks about the problems related to goodness of the fit of the model. Prob F-statistics is 0.00000 which means there is no problem in the model.

4.3.2 Fixed Effect Model: Impact of GI on ROA

Table 4.6: Redundant Fixed Effects Tests

Effects Test	**Statistic**	**d.f.**	**Prob.**
Cross-section F	7.0953	-39283.0000	0.0000
Cross-section Chi-square	223.6914	39.0000	0.0000

Table 4.7: Impact of GI on ROA

Variable	**Coefficient**	**Std. Error**	**t-Statistic**	**Prob.**
C	-0.1091	0.0391	-2.7926	0.0056
GI	0.0257	0.0124	2.0711	0.0393
CAP	0.0251	0.0132	1.8955	0.0590
LOANS	0.0336	0.0099	3.3756	0.0008
DEP	-0.0194	0.0121	-1.5993	0.1109
SZ	0.0074	0.0018	4.1285	0.0000
Effects Specification Cross-section fixed (dummy variables)				
R-squared	0.5991	Mean dependent var	0.0050	
Adjusted R-squared	0.5368	S.D. dependent var	0.0188	
S.E. of regression	0.0128	Akaike info criterion	-5.7541	
Sum squared resid	0.0463	Schwarz criterion	-5.2337	
Log likelihood	988.6679	Hannan-Quinn criter.	-5.5465	
F-statistic	9.6115	Durbin-Watson stat	1.2932	
Prob(F-statistic)	0.0000			

Results shows that the country level governance negatively affect the bank performance. Fixed effect model is used to elaborate the impact of independent variables on bank performance. The p-value of GI is (0.0393) which is less than from (0.05) and coefficient value is (0.025653). It means that GI positively and significantly effect on Return on assets. Some bank specific variables are included in this regression equation. The capital of banks has significant p-value (0.059) with its coefficient value (0.025104). It means that when banks have higher capital it will positively and significantly effect on ROA which means high capital leads to higher bank performance. Loans have positive coefficient (0.033559) and p-value is (0.0008) which is less than from (0.05). It means that when banks advance loans it will positively affect the Return on Assets. The p-value of deposits is (0.1109) which is less than from (0.05) and coefficient value is (-0.01941). This result show that when banks have more deposits it will negatively and insignificantly affect the

ROA. The size of banks has significant p-value (0.0000) with its coefficient value (0.0073). It means that when banks have larger size it will positively and significantly affect ROA. The bank size is the always discussing point in the banking sector. It indicates that more assets positively affect the bank performance.

Moreover, the R-squared value build a suitable source for the model of GI and bank performance. In next section con banks data set results shows that value of R2 (0.5990) which mean that dependent variable bank performance only 59% influenced through these independent variables Country level governance. Adjusted R-square value is (0.5367). Explanatory power of model is low which is usually on lower side in these types of studies. F-statistics talks about the problems related to goodness of the fit of the model. Prob F-statistics is 0.00000 which means there is no problem in the model.

4.3.3 Fixed Effect Model: Impact of GI on ROE

TABLE 4.8: Impact of GI on ROE

Variable	**Coefficient**	**Std. Error**	**t-Statistic**	**Prob.**
C	-5.1816	2.5160	-2.0595	0.0404
GI	1.057587	0.507766	2.082822	0.0389
CAP	3.3518	0.8565	3.9132	0.0001
LOANS	0.8228	0.6395	1.2865	0.1993
DEP	0.4498	0.7812	0.5758	0.5652
SZ	0.2746	0.1151	2.3851	0.0177
Effects Specification				
Cross-section fixed (dummy variables)				
R-squared	0.2461	Mean dependent var		0.0165
Adjusted R-squared	0.1284	S.D. dependent var		0.8809
S.E. of regression	0.8224	Akaike info criterion		2.5741
Sum squared resid	190.7387	Schwarz criterion		3.0956
Log likelihood	-375.8573	Hannan-Quinn criter.		2.7822
F-statistic	2.0918	Durbin-Watson stat		1.4021
Prob(F-statistic)	0.0002			

Results show that the country level governance positively influenced ROE. Random and fixed effect model is used to elaborate the impact of independent variables on bank performance. The p-value of GI is (0.0389) which is less than from (0.05) and coefficient value is (1.057587). It means that GI positively and significantly effect on ROE. Some bank specific variables are included in this regression equation. The capital of banks has significant p-value (0.0001) with its coefficient value (3.3518). it means that when banks have higher capital it will positively and significantly effect on ROE which means high capital leads to higher bank performance. Loans have positive coefficient (0.822) and p-value is (0.1993) which is above than from (0.05). It means that when banks advance loans it will positively affect the ROE. The p-value of deposits is (0.565) which is less than from (0.05) and coefficient value is (0.449). This result show that when banks have more deposits it will positively and significantly affect the bank performance. Deposits are the one of main earning sources for banks. The size of banks has significant p-value (0.017) with its coefficient value (0.274585). It means that when banks have larger size it will positively and significantly affect ROE. The bank size is the always discussing point in the banking sector. It indicates that more assets positively affect the bank performance.

Chapter 5

Conclusion

Sometimes banks have to face a remarkable volume of governance issues regarding toward content of different policy and timing. The governance of any country may affect its business activities as the literature presented above has proved. Empirical literature has showed that good governance play a very crucial role in maximizing profits along with it I, governance also minimize agency problems in firms. For promoting a fair regulatory framework, justice, legitimacy and market openness a good country level governance is crucial that results into better and strong economic activates, transparency in the economy and sound business environment (Avram, Grosanu & Rachisan, 2015). A good governance affect company‘s reputation and attract investors that ultimately increasers company‘s profits. However, the current study explored the influence of country-level governance on bank‘s profitability in Pakistan. The performance of private banks as compare to public banks is much better as the practices of country level governance in private banks are positive and better as compare to public banks of Pakistan.

Number of studies have been conducted to the profitability in banks and its influence of bank-specific (internal determinants) and macro-economic (external determinants) on in some of under developed countries such as in India (e.g., Al-Homaidi et al., 2018; Almaqtari et al., 2018; Bapat, 2017; Maiti& Jana, 2017; Almaqtari, Farhan, Thabit, & Al Homaidi, 2020; Sinha& Sharma, 2016; Al-Homaidi, Almaqtari, Yahya, &Khaled, 2020). Thie current research is mainly conducted in Pakistan and it used data of 42 commercial banks of Pakistan from 2006 to 2019. Moreover, It measures for profitability and the six dimensions of the Worldwide

Governance Indicators, as discussed earlier in this paper (1) voice and accountability, (2) political stability and absence of violence, (3) government effectiveness, (4) regulatory quality, (5) rule of law and (6) control of corruption were employed as proxies for country-level governance. Prior literature revealed that performance of private banks is better as compare to public banks however the influence of country level governance in private bank‘s profitability is positive and much better as compare to profitability of public banks.

Three measures are used in this study. First dependent variable measure is Return on assets results shows that country level governance positively affects ROA. Due to better governance ROA increase means that assets utilization is better. Capital and loan positively affect the ROA means that capital increases return on assets increases while loan increases customer increases due to this return on assets rises. On the other hand deposits negative effect ROA show that when deposits increase and bank can’t expand or utilized theses deposits negatively affect the bank performance. Assets Size is an important for any organization. When banks more assets shows banks performance increases.

Second dependent variable is Return on equity. Country level governance positively affects the ROE. It show when there is no problem in governance means the utilization of equity is being conducted on better way. Banks performed under the good governance showed good performance. Good performance of acompany can attract investors and other potential users and lead organization to high values as it’s a fundamental point of view however, bad company performance can lower its share value. Company’s performance is also a result of company’s formal efforts which reflects the efficiency and the effectiveness of company‘s activities in a certain period.

Control variables are positively associated with ROE. It shows that when banks increase their capital then equity increases. It leads to higher bank performance. Next variables are loan and deposits results show that when loan and deposits increases it will leads to higher return on equity. Third variable is NIM which is negatively affected by country level governance. It shows the governance effect net income of the banks.

5.1 Policy Recommendation

The findings of the present study provide vital information to policymakers, regulators, bankers, financial analysts, and academicians in Pakistan. The research identifies a critical profitability problem, proposes policy and regulatory solutions, and provides a scientific course of action. In case of NIM all independent variables (capital, deposits, loans, and size) except GI has positive significant effect on NIM (Net interest Margin) GI (Government index) has insignificant positive impact on NIM. On the other hand all independent variables has significant positive effect on ROA (Return on Assets)but deposits has insignificant negative effect on ROA. In case of ROE(Return on Equity) all results has positive significant effect on ROE but loans and deposits has insignificant positive effect on ROE. In light of the results of the present study, regulations and several policy measures could be introduced to improve the profitability of Pakistani banks. Promoting greater transparency and better accountability, strong rule of law and judicial enforcement, better regulatory quality and vital control of corruption could be encouraged which could enhance higher profitability for Indian banks. Hence, it is vital for relevant stakeholders to contrive practical policy frameworks that reconsider the dimensions of country-level governance to avoid poor governance practices and lower profitability. Strategies on corporate level should be precise so that new opportunities cannot be spoiled, and threats are either eliminated or neutralized.

5.2 Limitation

Thus, this study's first restriction is related to the limited period 2006-2019 because of the difficulty of finding accessible data for a more extended period in most countries. Although this study gives the extensive understanding about country level governance and bank performance of commercial banks of Pakistan, but this study is only limited to Pakistan and does not cover the all aspects. This study is a country specific because it is only limited to the Pakistan.

5.3 Future Research

This study may serve as a key step to further research. The study focused on performance of the commercial bank of Pakistan. It recommended that many other countries should be selected for impact of CGI on commercial bank performance and should cover the large set of banking sector. This research can be extent on more Asian developing countries like Pakistan, India Bangladesh Nepal Bhutan. In this research estimate separate analysis can be done of Islamic and conventional banks. The time frame for research work, including the ten years from 2006 to 2019, this time period can be increased by 13 years for more accurate results. Research the sample size and time period of the data may be increased by taking into account remaining firms of different sectors in future.

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