The Nexus Between Corporate Governance and Financial Performance: A Review from Periods of Financial Distress

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Abstract

Companies are highly vulnerable to financial distress resulting from disruption events because most business activities involve macroeconomic aspects such as exchange rate, interest rate, and economic growth. Financial distress has the effect of disrupting supply-chains, reducing purchasing power, and decreasing firm performance. This paper presents a summary of current studies on the topic of practicing corporate governance to maintain firm financial performance in times of financial distress in developed and developing countries. Most previous research utilized panel regression which consisted of pooled, random and fixed-effect models. Financial distress has a negative impact on profitability and stock price on the stock exchange. There are three corporate governance strategies that increase financial performance such as boards independence, meetings, and audits. Furthermore, board size and large shareholders caused negative impacts on firm financial performance. Although the application of corporate governance is considered to be effective in maintaining performance during financial distress, we failed to find consensus among the empirical evidence to demonstrate that governance practices boost financial performance during financial distress. These findings suggest that there is need for further research to provide empirical evidence of the effects of corporate governance on financial performance during periods of financial distress.

Keywords: corporate governance, profitability, financial distress, non-financial firms

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