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### Cooperate governance and firm cash holdings: A comparison between banks and insurance companies in Nigeria

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#### Abstract

The research study considered corporate governance and firm cash holdings: a comparison between bank and insurance companies in Nigeria. The research design adopted for the study is expo factor research design. The population of the study consists of all the 16 banks and 40 insurance companies quoted in the Nigeria Stock Exchange as at December 2018. A sample of 11 banks and insurances companies each was selected base on their size from the population of the bank and insurance companies. Data for the study were obtained from annual reports for the period of ten (10) years ranging from 2009 to 2018. Regression analysis E-View 7.0 was used to establish the existent of relationship in the variables while the Independent sample test was used to compare the differences in cash holding in the bank and insurance companies in Nigeria. It was established that no significant relationship exist between corporate governance and firm cash holdings in bank sector in Nigeria as well as that of the insurance companies sector. However, there is significantly difference in the number of directors in the banking sector than those in the insurance sector. Also, the study reveals that accounts receivables in the banking sector is significantly higher than that reported in the insurance sector, while, cash & cash equivalent and financial asset, has no significant difference between insurance and banking sectors. It was therefore recommended among other that while continuous reforms in corporate governance are commendable but much still need to be done by the government, to ensure that the international codes of corporate governance should be adhered to due to the complexity and constant changing environment and to meet the need of Nigerian governance environment.

**Keywords:** *Corporate governance, cash holdings, accounts receivables*

#### Introduction

Cash is the most liquid asset and is a measure of a companies' ability to pay its bills on time. Although holding of cash is important to pay off obligations, idle cash does not earn anything. (Zhang, 2016) <sup>[67]</sup>. (Yu, Lee, & Fok, 2015) <sup>[66]</sup> added that firms need to build up cash reserves by ensuring that the timing of cash movements creates an overall positive cash flow situation. Thus, an optimal level of cash based on the firm's needs is the essential ingredient that enables a business to survive and prosper as (Gill & Shah, 2012) <sup>[31]</sup> maintained. It has always been a critical problem in a company to decide an appropriate amount of cash for day-to-day operation of the business as opted by (Wasiuzzaman, 2014) <sup>[65]</sup>. The decision of how to deploy internal funds is central to the conflict between shareholders and managers (Jensen, 1986) <sup>[41]</sup>. Any discussion of the efficacy of corporate governance mechanisms to control managers must address this issue. During an economic expansion, as cash reserves increase, managers make strategic decisions about whether to disburse the cash to shareholders, spend it internally, use it for external acquisition, or continue to hold it. (Wang, 2015) <sup>[25]</sup> noted that it is theoretically not clear how self-interested managers will choose between spending free cash flow and stockpiling it as cash reserves. Managers must trade off private benefits of current spending against the flexibility provided by accumulating excess cash reserves. Further, self-interested managers must weigh whether the likelihood of discipline is greater from excess spending or from visibly holding too much cash. (Uyar, & Kuzey, 2014) <sup>[62]</sup>

(Venkiteshwaran, 2011) <sup>[63]</sup> pointed out that over the years, it has always been a crucial issue to decide an appropriate cash level in companies. As emphasized in finance literature there are three motives of holding money which are transaction motives: cash required by a firm to meet the day to day business operations; precautionary motives: to meet the contingencies or unforeseen circumstances arising in the course of business and speculative motives: to avail the benefit of bargain purchases that may arise in the future. (Tong, 2006) <sup>[61]</sup> affirm that optimum level of cash holding is the fundamental of sufficient liquidity. (Subramaniam, Tang, Yue, & Zhou, 2011) <sup>[60]</sup> submitted that liquidity refer to whether or not an organization is in a position to meet its short-term obligations as they fall due. (Schauten, Dick & Waal, 2008) <sup>[59]</sup> agrees that for that reason, every firm should maintain optimum cash balance in order to meet the day to day operations. The management should also consider the factors determining and influencing the cash balances at various point of time. (Liu, Lou, & Tian, 2015) <sup>[47]</sup> added that finance pioneers recommended that the cost of excess cash and danger of inadequate cash should be matched to determine the optimum level of cash balances. (Masood, & Shah, 2014) <sup>[50]</sup>, affirm that there are many reasons in firms to hold cash: to warrant the operations, meet up obligations, and take hold of the good investment opportunities. Further, optimum level of cash acts as a protection to prevent high opportunity costs during cash shortage in the firms (Ozkan & Ozkan, 2004).

Why sufficient amount of cash and cash equivalents are required to be held by the firms as avow by (Sadegh, Kangarlauei, Soleymani, & Motavassel, 2013) <sup>[56]</sup>. Many reasons have been given about firms that hold cash and equivalents of cash. Due to insufficient cash there can be low financing costs for the firms. (Pinkowitz, Stulz, & Williamson, 2006) <sup>[55]</sup> affirm that this could be the main reason that why the firms like to hold the cash. (Đinh, & Anh, 2013) <sup>[20]</sup> maintain that managers may use cash for their own needs without caring of shareholders. In other words they may see their benefit and it may annoy the shareholder whose cash is being used. It has also been reported that firms that obtain more volatile earnings may have higher costing for external financing. (Daher, 2010) <sup>[19]</sup>

A vast body of literature exists that has documented that firms hold too much cash than is required (Ditmar, & Smith, 2007; Drobetz, & Gruninger, 2007; Khalil, & Ali, 2015; Liu, *et al.* 2015). For instance, (Bates, Kahle, & Stulz, 2009) <sup>[24]</sup> documented that U.S. firm's cash ratio has more than doubled from 1980 to 2006. Various explanations are provided for corporate cash holdings such as precautionary motive, transactional motive, research & development intensity (Chireka, & Fakoya, 2017), agency theory (Jensen, 1976) <sup>[42]</sup>. These motives argue that firms hold cash for operational and investment opportunities while the agency theory argues that firm's level of corporate cash holdings is influenced by the agency conflicts between managers and shareholders as managers have an incentive to hold more cash as they tend to pursue private benefits (Kim, Kim, & Woods, 2011; Harford, Mansi, & Maxwell, 2008) Corporate governance is a uniquely complex and multi-faceted subject. Devoid of a unified or systematic theory, its paradigm, diagnosis and solutions lie in multidisciplinary fields including: economics, accountancy, finance among others (Liu, Luo & Tian, 2015; Anabestani, & Shourvarzi, 2014) <sup>[47]</sup>. It is therefore essential that a comprehensive framework be codified in the accounting structure of any organization. (Chang, Chou, & Huang, 2014) added that corporate governance is one of the several key factors that determine the health of the system and its ability to survive economic shocks. The health of the organization depends largely on the underlying soundness of its individual components and the connections between them. Against the above backdrop, this study is undertaken with a view to ascertain corporate governance and firm cash holdings: a comparison between bank and insurance companies in Nigeria.

### Objectives of Study

The main objective of the study is to determine corporate governance and firm cash holdings: a comparison between bank and insurance companies in Nigeria. The specific objectives of this study are:

1. To ascertain the relationship between corporate governance and firm cash holdings in fin banking sector in Nigeria.
2. To ascertain the relationship between corporate governance and firm cash holdings in the insurance sector in Nigeria.
3. To determine the significant difference in cash holding in the bank and insurance companies in Nigeria

### Research Questions

To achieve the specific objectives of this study the following research questions were raised:

1. To what extent is the relationship between corporate governance and firm cash holdings in bank sector in Nigeria?
2. What is the relationship between corporate governance and firm cash holdings in insurance sector in Nigeria?
3. What is the significant difference in cash holding in the bank and insurance companies in Nigeria?

### Conceptual Review

#### Corporate Governance

Corporate governance is a concept that emerged following the growth of corporations in the 20th century, and in particular, following the stock market crash in 1929, which led scholars to argue for corporate governance mechanisms that would allow shareholders to keep companies in check (Ogundipe, Ogundipe, & Ajao, 2012). A lot of scholars however attribute the considerable interest in corporate governance practices in modern corporations to the high profile collapse of a number of large firms in the US such as the Enron Corporation (Alagathurai & KGA, 2017).

Corporate governance is simply defined as the acceptance by management of the alienable rights of shareholders as the true owners of the corporation and their role as the trustees on behalf of the shareholders (Azmat, 2011).

(Anabestani, & Shourvarzi, 2014) defines corporate governance as the structures and processes for the direction and control of companies; in order words, corporate governance concerns the relationship amongst the management, board of directors, controlling shareholders, minority shareholders and other stakeholders.

(Chen, & Chuang, 2009) opines that corporate governance serves two major indispensable purpose which are to enhance the performance of corporations by establishing and maintaining a corporate culture that motivates directors, managers and entrepreneurs to maximize the company's operational efficiency thereby ensuring returns on investment and long-term productivity. it ensures the conformance of corporations to laws, rules and practices which provide a mechanism to monitor directors' and managers' behaviour through corporate accountability that in turn safeguards the investor interest.

Corporate governance as the term implies is a mechanism that is employed to reduce the agency cost that arises as a result of the conflict of interest between managers and shareholders. The role of corporate governance according to (Sadegh, *et al.* 2013) is to reduce the divergence of interests between shareholders and managers. It remains one of the most important determinants in ensuring the quality of the financial reporting process. It is a set of mechanisms that affect how a corporation is operated. It deals with the welfare and goals of all the stakeholders, including shareholders, management, board of directors, lenders, regulators, and the economy as a whole (Opler, Lee, Rene, & Rohan, 2001).

(Al-Najjar, 2013) came up with a corporate governance model in which he states that the main principles of corporate governance are consistency, responsibility, accountability, fairness, transparency and effectiveness. He goes further to add that his model's backbone hinges on four main areas- the right people (members of the board ought to be those that have competent skills, experiences a d knowledge), the right team (the board as a whole should consist of capable individuals), the right processes should be in place and there must be improvement in business

results. Similarly, (Gao, Harford, & Li, 2013) conducted a study on the determinants for success of corporate governance in an organization, some of which include a working board which will represent the interest of shareholders in truth and spirit, transparency in the organisation, sound whistle blowing system, balance in power, formal and periodic evaluation of the CEO, formal and periodic evaluation of directors, strong market institution, external regulation & monitoring, disclosure of compensation policies & practices, open and well implemented conflict of interest policy and condor between executives of a firm and staff. Based on these, (Gao, *et al.*) concluded that the adoption of corporate governance principles in an organisation is a huge step toward creating safeguards against corruption and mismanagement.

### **Cash holding**

Cash reserves give firms much needed financial independence, thereby enabling them to follow their strategic trajectory with limited external interference (Bigelli, & Sánchez-Vidal, 2012). Furthermore, internally generated funds are cheaper than those externally sourced. As such, firms with sufficient cash in hand can invest in viable investment opportunities at a low cost of financing. Stockpiling cash reserves, however, might unintentionally fuel inefficiencies involving the use of corporate resources. (Ali, & Yousaf, 2013) argue that sufficient liquid assets afford managers the flexibility to use these resources even in negative net present value (NPV) projects. Recent studies by (Faulkender, & Wang, 2006; Dittmar, & Mahrt-Smith, 2007)<sup>[64]</sup> have confirmed Jensen's (1986)<sup>[41]</sup> free cash flow hypothesis that an additional dollar that a firm hold is less than one dollar. (Daher, 2010)<sup>[19]</sup> posits that underlying these findings is the assumption that excessive cash conceals the benefits of externally sourced funds as the monitoring tool, as well as allowing managers to extract personal advantages. (Ferreira, & Vilela, 2004), cash holdings, therefore, have both an upside and a downside so that firms need to maximize the former while minimizing the latter.

In perfect markets with no information asymmetry, taxes, and agency and transaction costs, companies have no need to hold cash, as there are no benefits or costs of allocating cash. When internal cash owned by the firm is not sufficient to meet the needs, the company can obtain external financing at fair prices that do not compromise growth and investment (Gill, & Shah, 2012)<sup>[32]</sup>. In such a frictionless world, cash holdings would have no effect on the firm value or shareholder wealth (Opler *et al.*, 2001). Markets are, however, imperfect, and these imperfections cause external financing to be more expensive than internal resources. Therefore, in the real world of imperfect markets, corporate cash holdings are a strategic component of the business capital structure. Firms with peculiar circumstances should decide on their optimal cash holdings level. (Gill, & Mathur, 2011)<sup>[32]</sup>

### **Motives of holding cash**

Further to the above theories, there are various other motives that influence firms to hold cash. The most outstanding, in literature, of these are the transaction motive, the precautionary motive, the tax motive and the speculative motive. These are discussed below.

### **The transaction motive**

The transaction motive is a classic model for optimal demand for cash, which gained popularity in the 60s with the major proponents being (Kuan, Li, C & Chu, 2011). The reasoning behind this motive is that in a case where a firm does not have cash to meet its financial obligations or to invest in profitable projects, the company either should approach the financial markets or to dispose of noncash financial assets to raise the finance needed. The cash required to make these payments is the optimal demand for cash. Unfortunately, these fundraising transactions can incur significant costs (Maxwell, 2008; Bates *et al.*, 2009). (Saddour, 2006) states that in a world of imperfect markets, a firm can circumvent transaction costs by increasing its cash holding

### **The precautionary motive**

Companies tend to retain more cash if they anticipate future cash flows to be volatile and access to capital markets to be costly (Bates *et al.*, 2009). (Pinkowitz, Stulz, & Williamson, 2006)<sup>[55]</sup>, if future cash flows are expected to be volatile, firms will increase their cash holdings as a way of hedging against future uncertainty. These differential cash holdings are known in the literature as precautionary cash holdings. (Almeida, Campello, & Weisbach, 2004) advocates that the precautionary motive is more relevant to financially distressed firms than to their unstressed peers. Firms that anticipate future difficulties in raising funds for investments and operations tend to retain high cash holdings as a safeguard (Al-Najjar, & Belghitar, 2011).

### **The tax motive**

The transaction motives and the precautionary motives have mostly been cited in the empirical literature to be driving corporate cash holdings, (Foley, Hartzell, Titman, & Twite, 2007) found evidence that repatriation taxes in part influenced the cash holdings of US transnational firms. The US imposes taxes on the income earned from the foreign operations of local businesses, although they award tax credits for the foreign taxes paid on the foreign operations. In this study, (Foley *et al.* 2007) found that US firms with foreign subsidiaries tend to hold the cash earned in the foreign subsidiaries to avoid taxes upon repatriation. These overseas subsidiaries will use their earnings to invest in positive NPV projects with the remainder of the earnings being kept as cash reserves. (Foley, *et al.* 2007) found that firms exposed to greater tax burdens on repatriated earnings will hold more cash. Although the findings of (Foley *et al.* 2007) apply to the US and many other countries, the South African tax laws are different.

### **The speculative motive**

Sometimes firms arm themselves with cash piles in anticipation of future profitable investment opportunities (Kariuki, Namusonge & Orwa, 2015). Although (Yu, Lee, Yi, & Fok, 2015)<sup>[66]</sup> find that previous period cash holdings by Chinese firms lead to increased speculative activities in the following year, the speculative motive of holding cash was also found to weaken, as the level of corporate governance improved. This is because, as the study explains, speculative activities are generally noncore and oftentimes unethical activities. As corporate governance is more pronounced in South Africa than in China due to the influence of institutional investors (Zhang, 2016)<sup>[67]</sup>, this study envisages that the speculative motive of cash holdings is

negligent in South African firms. Again, the difficulty of identifying and measuring risk activities inhibits the possibility of empirically investigating the speculative motive of cash holdings (Yu, *et al.* 2015).

### **The determinants of cash holdings**

#### **Firm size and cash holdings**

The nexus between corporate cash holdings and firm size has been debated extensively in many studies. (Al Zoubi, 2013). Per the trade-off theory, the relationship between firm size and cash holdings is negative. (Bigelli & Sanchez-Vidal, 2012) postulate that larger companies enjoy the economies of scale, which, in turn, enables these companies to secure external finance relatively quickly and cheaply. Moreover, more major companies utilize their economies of scale to lower transaction costs, which are fixed expenses incurred in external borrowing (Kim *et al.*, 2011). (Al-Najjar *et al.*, 2011), affirm that larger firms are more diversified than the smaller ones and so are less susceptible to bankruptcy cost. As transaction costs are lower for larger firms than smaller companies, firm size and cash holdings are expected to have an inverse relationship. The pecking order theory envisages a positive correlation between firm size and corporate cash holdings, as the former is viewed as a proxy for business success. Larger companies achieve growth through profitability and are likely to retain more cash after controlling for their investment needs (Ferreira & Vilela, 2004).

Furthermore, the agency theory posits that larger firms have dispersed shareholders, allowing more autonomy to the managers to hold more cash for private perquisites (Ferreira *et al.*, 2004).

#### **Leverage and cash holdings**

The trade-off theory postulates that high leverage exposes companies to financial distress and bankruptcy. Highly levered companies will, thus, have a precautionary motive to hold more cash to avert bankruptcy (Al-Najjar and Belghitar, 2011; Kim *et al.*, 2011). In contrast, (D'Mello, Krishnaswami, & Larkin, 2008) posit that leverage indicates a firm's ability to access the capital markets for more debt successfully.

Consequently, highly levered firms (with high ability to obtain extra debt from the markets) will hold less cash. The trade-off theory is, therefore, inconclusive regarding the relationship between leverage and cash holdings. (Gomes, 2012) The pecking order theory argues that debt grows when a firm's investment needs surpass its retained earnings (Ferreira, *et al.*, 2004). Therefore, highly levered firms will have less cash as their investment needs outweigh their cash-generating abilities, indicating a negative relationship between leverage and cash holdings. From an agency theory perspective, highly levered firms are less likely to hold high cash reserves because of the monitoring role of debt. (D'Mello, *et al.*, 2008)

Although some researchers found a nonlinear relationship between leverage and cash holdings (Drobetz & Gruninger, 2007; Guney *et al.*, 2007)<sup>[24]</sup>, most recent studies have found that highly levered firms tend to hold less cash (Al-Najjar & Belghitar, 2011; Subramaniam *et al.*, 2011; Uyar and Kuzey, 2014; Wasiuzzamam, 2014)<sup>[62]</sup>.

#### **Investment opportunities and cash holdings**

Per the pecking order theory, firms with high investment opportunities will hold more cash to lower the cost of financing

these investments, since internally generated funds are cheaper than capital market financing (Kim *et al.*, 2011; Bigelli & Sanchez-Vidal, 2012). On the other hand, the trade-off theory posits that firms with growth potential (investment opportunities) will be driven by the precautionary motive to hold more cash, as market constraints and financial distress will be costlier to such firms (Ferreira *et al.*, 2004; Kim *et al.*, 2011).

From an agency theory standpoint, low-growth firms (companies with fewer investment opportunities) but run by entrenched managers might still accumulate cash (Subramaniam *et al.*, 2011).

These managers will, in turn, use the cash holdings to invest even in negative NPV projects without being subjected to the scrutiny of the capital markets (Bates *et al.*, 2009).

#### **Liquid asset substitutes and cash holdings**

In the case of cash shortages, firms can convert their liquid assets into cash (Al-Najjar and Belghitar, 2011). Liquid assets can be turned into cash more cheaply than the other assets and can so help to avoid expensive capital market financing (Ozkan and Ozkan, 2004). The trade-off theory, thus, envisages a negative relationship whereby firms with higher liquid asset substitutes will hold fewer cash reserves.

#### **Capital expenditure and cash holdings**

Per the trade-off theory, capital investment mirrors financial distress (Bates *et al.*, 2009). Therefore, firms with high capital investment will face higher financial distress costs in the capital markets.

In their attempt to avoid these high transaction costs, such companies often hold more cash (Gomes, 2012). In contrast, capital expenditure usually results in the creation or the improvement of new assets that can be pledged by firms as collateral, thus, bolstering firms' borrowing capacity (Kim *et al.*, 2011). Consequently, companies that have enhanced access to loans will hold less cash.

#### **Dividend payments and cash holdings**

Per the trade-off theory, a negative correlation exists between dividend payments and corporate cash holdings levels, because firms that pay dividends can trade-off the high costs of stocking cash by drawing down on dividend payments (Al-Najjar, 2013). Companies that pay dividends can more quickly raise capital at lower costs in times of need by cutting down on dividend payments (Al-Najjar and Belghitar, 2011). (Drobetz, & Gruninger, 2007) posit that firms that pay dividends have better corporate governance mechanisms that, in turn, can raise capital at lower costs.

#### **Cash flows and cash holdings**

The trade-off theory views cash flow as an alternative source of liquidity than can set managers free from the financial constraints that can otherwise be imposed by the capital markets (Hardin Highfield, Hill, & Kelly, 2009). Essentially, cash flows can be used in times of cash shortages, thus, negating the need to hold cash (Kim *et al.*, 2011). The pecking order theory, however, proposes that firms with good cash flows will use these cash flows to finance their projects, pay off their debt and accumulate cash holdings.

Therefore, companies with persistently high cash flows will have significant cash holdings. While the two theories offer opposing views on the influence of cash flows on cash holdings (Islam, 2012).

### **Volatility of cash flows and cash holdings**

High volatility of cash flows signifies uncertainty in future earnings and, as such, a higher probability of financial distress (Ozkan and Ozkan, 2004). Since firms in financial distress might be forced to forego viable investment opportunities, these companies will hold more cash in line with the trade-off theory. The trade-off theory, therefore, envisages a positive relationship between cash flow volatility and cash holdings. (Isshaq, Bokpin, & Onumah, 2009)

### **Theoretical framework**

We expound the three theories of cash holdings that have been used to explain the pattern of cash holdings across various industries. The same arguments are expected to be relevant even to the banking and insurance sectors.

### **Trade-off theory**

We can identify two costs of holding cash and cash equivalents. If we assume that managers maximize shareholder wealth, the only cost of holding cash is the lower return earned on it, relative to other investments of the same risk. (Alim, Wajid & Khan, Safi Ullah, 2016). This cost is often called the cost-of-carry: the difference between the return on cash and the interest that would have to be paid to finance an additional dollar of cash. If we relax the assumption of shareholder wealth maximization, the costs of holding cash increase since managers now have the opportunity to engage in wasteful capital spending and acquisitions or, in some countries, outright theft (Iskandar-Datta, & Jia, 2014)

The benefits of holding cash balances stem from two motives. According to the transaction costs motive, firms hold more cash when the costs of raising it and the opportunity costs of shortfalls are higher, the current literature employs several variables to proxy for these costs. Given the substantial fixed costs involved in raising outside financing, small firms are likely to find it costlier to raise outside funds. In addition, there may be economies of scale in cash management, which also suggest that small firms hold more cash. (Ali, Ullah, & Ullah, 2016). Firms with better investment opportunities are expected to hold more cash because the opportunity cost of lost investment is larger for these companies; similarly, we expect firms with more volatile cash flows to hold more cash to protect against the higher likelihood of cash shortfalls. The level of capital spending, itself, should also be positively related with cash levels if it captures investment demands. In contrast, when cash flows are higher, firms need to hold less cash to meet future investment needs. (Cossin, & Hricko, 2004)

Finally, firms that pay dividends can always cut them to raise more funds, and they are therefore expected to hold less cash (Afza, & Adna, 2007), management with a goal to maximize shareholder wealth should aim to achieve an optimal cash holdings level by weighing the marginal benefits and marginal costs of holding cash. The advantages of holding cash derive from the transaction cost motive and the precautionary motive (Bigelli, & Sánchez-Vidal, 2012). By holding cash, firms cut down on the transaction cost of raising funds from the capital markets.

Furthermore, holding cash is a safeguard against difficult times when companies struggle to obtain funding from external sources (Fischer, Marsh, & Brown, 2014). Holding more cash, however, comes with a price, as businesses pay a liquidity premium in the form of the lower rate of return generated by these stored liquid assets. (Shah, 2012) posits that the main cost of holding cash is the opportunity cost of capital invested in liquid assets such as forfeited profitable investments (Ferreira *et al.*, 2004).

### **The pecking order theory**

Contrary to the trade-off theory's assertion of the existence of an optimal level of cash holdings, the pecking order theory as affirmed by (Faleye 2004) envisages that because of the asymmetric information between firms and capital markets, external funds are more expensive for companies than internally generated funds. To avoid high borrowing costs, companies will prefer to utilize internal resources to finance investments before looking for external funds in this order: safe debt, risky debt and, lastly, if needed, equity (Ferreira *et al.*, 2004).

### **The agency theory**

The agency cost (Jensen, 1986) <sup>[42]</sup> view of corporate cash holdings suggests that managers who are less concerned with shareholder wealth hoard cash and invest it in negative NPV projects or use it to overpay in acquisitions. Of course, simply holding too much cash destroys value because of the cost of risk. In addition, if these cash holdings reduce the discipline imposed on management, corporate decision making may be affected, resulting in reduced firm earnings. In financial management, the agency theory addresses the problems that often arise between the principal (shareholders) and the agent (management). (Jensen, & Meckling, 1976) <sup>[42]</sup>. The agent has the duty to act and conduct the firm's business in a way that maximizes shareholders' wealth. Researchers have found that, among other things, there can be a conflict between maximizing shareholders' wealth and maximizing management remuneration. Another conflict arises when the principal and the agent have contrasting risk outlooks (Dinh Pham Anh, 2013) <sup>[20]</sup>.

### **Empirical review**

(Dittmar, Maht-Smith & Servaes, 2003) collected a sample of more than 11,000 firms from 45 countries and found that corporations in countries where shareholders' rights are not well protected hold up to twice as much cash as corporations in countries with good shareholder protection. They also found that when shareholder protection is poor, factors that generally drive the need for cash holdings, such as investment opportunities and asymmetric information, actually become less important. In addition, the study found that firms hold larger cash balances when access to funds is easier and further stated that agency problems are important determinants of corporate cash holdings. Therefore, strong corporate governance is necessary.

(Drobetz, & Gruninger, 2007) <sup>[24]</sup> investigated the determinants of cash holdings for a comprehensive sample of 156 Swiss non-financial firms between 1995 and 2004 and they found a positive relationship between CEO duality and corporate cash holdings and a non-significant relationship between board size and corporate cash holdings. That is, CEO duality leads to significantly higher cash holdings and larger board size has no impact on corporate cash holdings.

(Kuan, Li, & Chu, 2011) examined the association between corporate governance and cash policy of family-controlled firms. The authors found that the impact of corporate governance, with its separation of control rights and cash flow rights, director-ownership-in-pledge ratio and proportion of independent directors on cash policy, differs between family-controlled and nonfamily-controlled firms. The authors also found that the separation of seat control rights and cash flow rights, as well as chair duality, significantly affects the cash policy within different levels of cash holdings in firms.

(Gill, & Shah, 2012)<sup>[31]</sup> sampled Canadian firms from 2009 to 2011 and found that CEO duality and board size positively impact corporate cash holdings. Hence, the board of directors and the CEO are responsible for formulating policies regarding cash management, accounts receivable, inventory purchases and maintenance, accounts payable, and all other policies in the organization. Thus, board size and CEO duality play an important role in the organization and may lead to, high cash balances; high volume of accounts receivable; high amount of accounts payable; and a fast cash conversion cycle. (Anabestani, & Shourvarzi, 2014)

The optimization of working capital balances helps minimize working capital requirements, which in turn, increase firms' free cash flow (Grinstein, Weinbaum, & Yehuda, 2008). Inefficient working capital management policy, induced by poor corporate governance, has a negative impact on shareholders' wealth. Effective corporate governance serves as a check on the management of the firm's resources.

The financing hierarchy view suggests that there is no optimal level of cash, just as there is no optimal level of debt. Cash balance are simply the outcome of the investment and financing decision made by the firm as suggested by the pecking order theory of financing (Dittmar *et al.*, 2003). However, (Guney, Ozkan, & Ozkan, 2007) suggest that firms will use internal fund before resorting to external fund because acquiring external fund incur cost such as transaction cost as well as those arising from information asymmetric. Therefore, firms with access cash flow might accumulate cash while firms that invest heavily will deplete the cash level.

(Dittmar & Mahrt-Smith (2007) examined how corporate governance impacts a firm's value by comparing the firm's value and their use of cash holdings between poorly governed and well-governed firms. They discovered that corporate governance has a substantial impact on firm value through its impact on cash holdings. Poorly governed firms dispel cash quickly, and it eventually reduces operating performance. However, a well-governed corporate governance firm that dispels larger cash holdings eliminates the negative impact on operating performance.

(Pinkowitz, Stulz & Williamson, 2006)<sup>[55]</sup> found that companies in 35 countries with limited protection for minority shareholders tend to have higher ratios of cash-to-total assets than comparable companies in more protective regimes. (Pinkowitz *et al.* 2006)'s findings also support Michael Jensen's "free cash flow" theory – the tendency of corporate managers in mature companies to retain and then waste excess cash on low-return projects. (Pinkowitz *et al.* 2006) also suggested that in companies facing significant agency costs of free cash flow, cash holdings should be discounted since they are expected to be spent partly on projects designed to increase the welfare of those who control the firm

rather than to maximize the wealth of all investors. (Harford, Mansi, & Maxwell, 2008) shows that regardless of a firm's level of corporate governance, firms with large cash reserves spend more on acquisitions. (Harford *et al.* 2008) build on this finding and show that poorly governed firms dissipate cash through acquisitions.

(Dittmar *et al.* 2003) found that corporate governance affects the level of cash holding using evidences from 45 countries. Specifically, manager prefers to hold more cash in countries with poor shareholder protection. In contrast, (Harford *et al.* 2008) suggested that poor governance results in less cash holdings. However, early literatures found that the relationship between cash holdings and firm-level corporate governance is not significant (Mikkelsen, & Partch, 2003). Furthermore, (Bates, Kahle & Stulz, 2009) also concluded that high cash holdings are resulted from preventing high risks of cash shortage, so that governance plays almost no roles in accumulating cash reserves. In another related study by (Gill & Shah, 2012)<sup>[31]</sup> studied 166 Canadian listed companies from 2008 to 2010. They found that cash holding is positively affected by CEO duality. One possible reason is that the CEO/Chairman does not act for the best interests of shareholders. This is in support with (Boubaker, Derouiche, & Nguyen, 2015) who agrees that with dual-responsibility, CEOs serve the interests of the management team and one way to protect the team's position is to hold excessive corporate liquidity.

The study of (Drobetz, & Gruninger, 2007)<sup>[24]</sup> investigate 156 Swiss non-financial firms from 1995 to 2004 also concluded the similar result. In contrast, study documented that duality leads to insider dominance that is similar to family control (Chen, Cheung, Stouraitis & Wong, 2005). Under agency theory, ineffective monitoring of board is one of the reasons for poor governance since there is little monitoring on managers and it is hard to fire poor performance directors (Chang, Chou, & Huang, 2014). Prior literatures suggest CEO duality seems to be less effective in corporate governance. Corporate with poor governance hold less cash as directors spend cash quickly. Corporate governance plays an important role in controlling the management of working capital by formulating sound policies and further added that CEO duality and board size help in maintaining an appropriate level of working capital in the organization The underlying reason is found in (Dittmar & Mahrt-Smith, 2007)'s study that excess cash holdings decrease the incentive to control cost or improve profit margins, and results in overinvestment in low margin projects.

According to agency theory, it is expected that non-executive director dominate board are likely to reduce agency cost and hence hold less amount of cash (Ozkan, & Ozkan, 2004). However, (Chen, & Chuang, 2009) found a positive relation between outside director and cash holdings since the nature of high-tech firms requires them to hold more cash for future investment.

(Chireka, & Fakoya, 2017), examine the determinants of corporate cash holdings levels among South African retail firms. With corporate cash holdings on the rise, stakeholders need to know, among other things, what informs the companies' cash holding policies and whether there are any benefits to be derived from piling up these cash reserves. Studies conducted in developed countries have identified the following as determinants of corporate cash holdings: firm size, growth

opportunities, liquid asset substitutes, capital expenditure, leverage, dividend payments, cash flows and cash flow volatility. Few studies have focused on what drives firms' cash holdings behavior in emerging economies. This study, the first of its kind, investigated the determinants of corporate cash holdings in the South African retail industry. The paper used panel data analysis to test the relationships between cash holdings level and the identified determinant factors. The authors found evidence that liquid asset substitutes, capital expenditure, dividend payments and cash flow volatility significantly influence the cash holdings levels of retail firms listed on the Johannesburg Stock Exchange. (Harford, Mansi, & Maxwell, 2008), study corporate governance and firm cash holding in the U.S., using governance metrics based on antitakeover provisions and inside ownership, we find that firms with weaker corporate governance structures actually have smaller cash reserves. When distributing cash to shareholders, firms with weaker governance structures choose to repurchase instead of increasing dividends, avoiding future payout commitments. The combination of excess cash and weak shareholder rights leads to increases in capital expenditures and acquisitions. Firms with low shareholder rights and excess cash have lower profitability and valuations. However, there is only limited evidence that the presence of excess cash alters the overall relation between governance and profitability. In the US, weakly controlled managers choose to spend cash quickly on acquisitions and capital expenditures, rather than hoard it. In a related study by (Alim, & Khan, (2016), examine corporate governance and its impact on firm's cash holdings in the context of the family-controlled firms and stand-alone firms in Pakistan, employing several measures of corporate governance. Empirical results show that family-controlled businesses hold more cash as compared to stand-alone firms, possibly alluding to the more prevailing agency problems between controlling shareholders and the minority shareholders. Results further shows that managerial ownership has a significant negative relationship with corporate cash holdings; big-five ownership is positively related to cash holdings while board size, CEO duality and institutional shareholders have no effect on firm's cash holdings. Overall, these results are consistent with the agency predictions of Jensen and Mackling (1986)<sup>[42]</sup> that higher managerial stakes provide managers with incentives to hold optimum levels of cash holdings. Results also support the view that institutional activism is low in Pakistan's market providing institutional shareholders less incentives to monitor firm's financial decisions.

## Methodology

### Research Design

The research design adopted by the study was expo facto research design.

### Population of the Study

The population of the study consists of all the 40 insurance companies and 20 commercial banks with international, National and Regional authorization quoted by Nigeria Stock Exchange as at December 2019

### Sample of the Study

The 11 insurance and banks companies were selected by using random sampling technique base on their size and the technique

gives each member of the population an equal chance of being selected

### Method of Data Analysis

The study employs parametric statistical techniques using multiple regression analysis techniques for testing hypotheses 1 and 2 while the t-test of independent samples was use for testing hypothesis 3.

### Model Specification

$$\text{CORGOV} = f(\text{CAEQ}, \text{ACRECE}, \text{FINASST},)$$

Where:

CORGOV = Corporate Governance (numbers of Directors)

CAEQ = Cash and cash equivalent

ACRECE = Account receivables

FINASST = Financial assets

The econometric form of the model is as follows:

$$\text{CORGOV} = b_0 + b_1 \text{CAEQ} + b_2 \text{ACRECE} + b_3 \text{FINASST} + \mu_t$$

### T-test of independent

To determine the difference in cash holding in the bank and insurance companies in Nigeria, the t-test of independent samples is employed to testing hypothesis 3.

### Data presentation and analysis of results

**Hypothesis one:** Ho1: There is no significant relationship between corporate governance and firm cash holdings in bank sector in Nigeria

### Data Presentation and Analyses of Results

**Table 1:** Ordinary Least Squares Result for Banks

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	14.14289	1.033980	13.67811	0.0000
CAEQ	5.36E-09	4.56E-09	1.176968	0.2422
FINANASSET	1.60E-09	1.43E-08	0.112103	0.9110
ACRECE	-1.38E-09	1.76E-09	-0.784974	0.4344
AR (1)	0.741858	0.068948	10.75962	0.0000
R-squared	0.562539	Mean dependent var		14.05051
Adjusted R-squared	0.543924	S.D. dependent var		3.114724
S.E. of regression	2.103479	Akaike info criterion		4.374247
Sum squared resid	415.9145	Schwarz criterion		4.505314
Log likelihood	-211.5252	Hannan-Quinn criter.		4.427277
F-statistic	30.21913	Durbin-Watson stat		2.347146
Prob(F-statistic)	0.000000			

Source: Author's Computation (2020) Using E-View 7.0

The ordinary least squares result in table 1 for banks shows that Cash and cash equivalent (CAEQ) has a positive relationship with CORGOV. The t-statistics is 1.18 and highly insignificant even at 5% level. Financial asset (FINASST) is positively signed and insignificant at 5% level. Its coefficient is 5.36E-09. ACCTS was negatively signed and insignificant at 5%. We therefore accept the null hypothesis. However, the result of the relationship may have bee influence by the skills and expertise of the directors of the firms that were featured in the study. Directors with better finance skills tend to achieve a more significant relationship and vice versa.

In measuring the explanatory power of the model, the adjusted R-squared showed that the model explain up to 54% systematic variation in Cooperate Governance. This leaves 46% unexplained

variation which may be captured by institutional factors. The F-statistics which measures the robustness of the variables put together indicates a high level of significance at 1% and thus shows that the explanatory variables have been well and carefully selected.

### Testing of Hypothesis 2

There is no significant relationship between corporate governance and firm cash holdings in insurance sector in Nigeria.

**Table 2:** Ordinary Least Squares Result for Insurance companies

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	9.002619	0.447152	20.13324	0.0000
ACRECE	-2.57E-11	2.89E-09	-0.008914	0.9929
CAEQ	-1.68E-11	5.50E-10	-0.030545	0.9757
FINASS	-2.59E-10	1.60E-09	-0.161888	0.8716
AR (1)	0.829900	0.048198	17.21865	0.0000
R-squared	0.656061	Mean dependent var		9.061728
Adjusted R-squared	0.647298	S.D. dependent var		1.594600
S.E. of regression	0.947012	Akaike info criterion		2.759369
Sum squared resid	140.8027	Schwarz criterion		2.854665
Log likelihood	-218.5089	Hannan-Quinn criter.		2.798060
F-statistic	74.86907	Durbin-Watson stat		2.375785
Prob(F-statistic)	0.000000			
Inverted AR Roots	.83			

Source: Author's Computation (2020) Using E-View 7.0

The ordinary least squares result in table 2 for insurance companies shows that ACRECE Account receivables (ACRECE) have a negative relationship with Corporate Governance (CORGOV). The t-statistics is -0.01 and highly insignificant even at 5% level. CAEQ is negatively signed and insignificant at 5% level. Its coefficient is 1.68E-09. FINASS was negatively signed and insignificant at 5%. We therefore accept the null hypothesis. In measuring the explanatory power of the model, the adjusted R-squared showed that the model explain up to 65% systematic variation in Cooperative Governance. This leaves 35%

unexplained variation which may be captured by insurance factors. The F-statistics which measures the robustness of the variables put together indicates a high level of significance at 1% and thus shows that the explanatory variables have been well and carefully selected.

### Hypothesis Three Ho3

There is no significant difference in cash holding in the bank and insurance companies in Nigeria.

**Table 3:** Analysis of Cash Holding of Bank and Insurance Companies in Nigeria Banks in Nigeria Insurance in Nigeria

S/N	Name of company	Year	Amt on CAEQ (N)	S/N	Name of company	Year	Amt on CAEQ (N)
1	First Bank plc	2009-2018	5,039,657,000	1	Allco Insurance American Inter. Plc	2009-2018	67,844,495
2	Access Bank plc	2009-2018	3,441,338,540	2	Consolidated Hallmark Insurance Plc	2007-2016	17,635,066,053
3	FCMB Bank plc	2009-2018	1,336,793,751	3	Cornerstone Insurance Plc	2009-2018	35,022,094
4	Diamond Bank plc	2009-2018	2,463,405,026	4	Custodian & Allied Insurance Plc	2009-2018	149,880,466
5	GTB Bank plc	2009-2018	2,144,649,476	5	Sovereign Trust Insurance plc	2009-2018	16,878,903
6	Stanbic IBTC Bank Plc	2009-2018	1,064,271,000	6	NEM Insurance Plc	2009-2018	25,391,182
7	Union Bank plc	2009-2018	1,193,624,000	7	Niger Insurance Plc	2009-2018	1,321,694
8	United Bank for Africa Plc	2009-2018	1,423,835,000	8	Lasaco Assurance Plc	2009-2018	33,270,908
9	Wema Bank plc	2009-2018	364,750,710	9	Staco Insurance Plc	2009-2018	24,455,525
10	Zenith Bank plc	2009-2018	5,601,806,000	10	Standard Alliance Insurance Plc	2009-2018	6,062,835
11	Sterling Bank plc	2009-2018	936,179,939	11	Regency Alliance Insurance Plc	2009-2018	89,439,104

Source: Researchers' compilations (2020)

The data above was use in testing hypothesis 3 and results is as presented in table 4

**Table 4:** T-Test results

	Types	Mean	Std. Deviation	t	p
NOS OF DIR	Insurance	90.94	13.48	-7.236	0.000
	Bank	140.82	23.82	-6.352	
CASH & EQUIV	Insurance	1018746259.00	4147030284.00	0.035	0.972
	Bank	973767330.50	1219710171.00	.043	
ACCTS RECEIV	Insurance	563178766.10	2297905798.00	-2.274	0.031
	Bank	3303316096.00	4217579963.00	-1.982	
FINANCIAL ASSET	Insurance	119191086.90	292958982.60	0.564	0.577
	Bank	66653685.18	117710901.40	.677	

*Source:* Author's Computation (2020) Using E-View 7.0

The above table shows that the number of directors in the banking sector is significantly higher ( $p < 0.05$ ) than those in the insurance sector. Also, the accts receivables in the banking sector is significantly higher ( $p < 0.05$ ) than that reported in the insurance sector. However, cash & cash equivalent and Financial asset, there was no significant difference ( $p > 0.05$ ) between insurance and banking sectors.

## Conclusion and Recommendations

### Conclusion

The purpose of this study is to determine the significant relationship in corporate governance and firm cash holdings: a comparison between bank and insurance companies in Nigeria, and also, to examine whether there is difference in cash holding in the bank and insurance companies in Nigeria. The continuous survival and stability of the banks and insurance companies sectors depends largely on the quality of its corporate governance cash holding among other factors. Hence, more effort is desirable to ensure adequate compliance to corporate governance code, as well as its attractiveness and effectiveness in improving performance. This present study found out that no significant relationship exist between corporate governance and firm cash holdings in bank sector in Nigeria as well as that of the insurance companies sector. However, there is significantly difference in the number of directors in the banking sector than those in the insurance sector. Also, the study reveals that accts receivables in the banking sector is significantly higher than that reported in the insurance sector, while, cash & cash equivalent and Financial asset, has no significant difference between insurance and banking sectors.

### Recommendations

Based on findings, the study recommends the following;

1. Management of insurance and bank companies in relation to their corporate governance should ensure that holding large amount of cash will help the ultimate goal of the business which is to maximise shareholders wealth and act in the best interest of all stakeholders. As good corporate governance system is used to make sure that the management of the company can run the company in the best interest of all stakeholders.
2. While continuous reforms in corporate governance are commendable, nevertheless, much still need to be done by the government. The Financial Reporting Council of Nigeria (FRC) should ensure that the international codes of corporate governance should be adhered to due to the complexity and constant changing environment of the banking and insurance sectors in Nigerian and to meet the need of Nigerian governance environment.
3. Relevant governmental bodies should also design a requirement to ensuring that appointed directors have the fundamental knowledge in finance. Where there are directors with deeper knowledge in finance, the cash holding of the firm tends to be at that point where the firm can meet its day to day business requirements and also be able to invest in projects which have positive net present values.

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