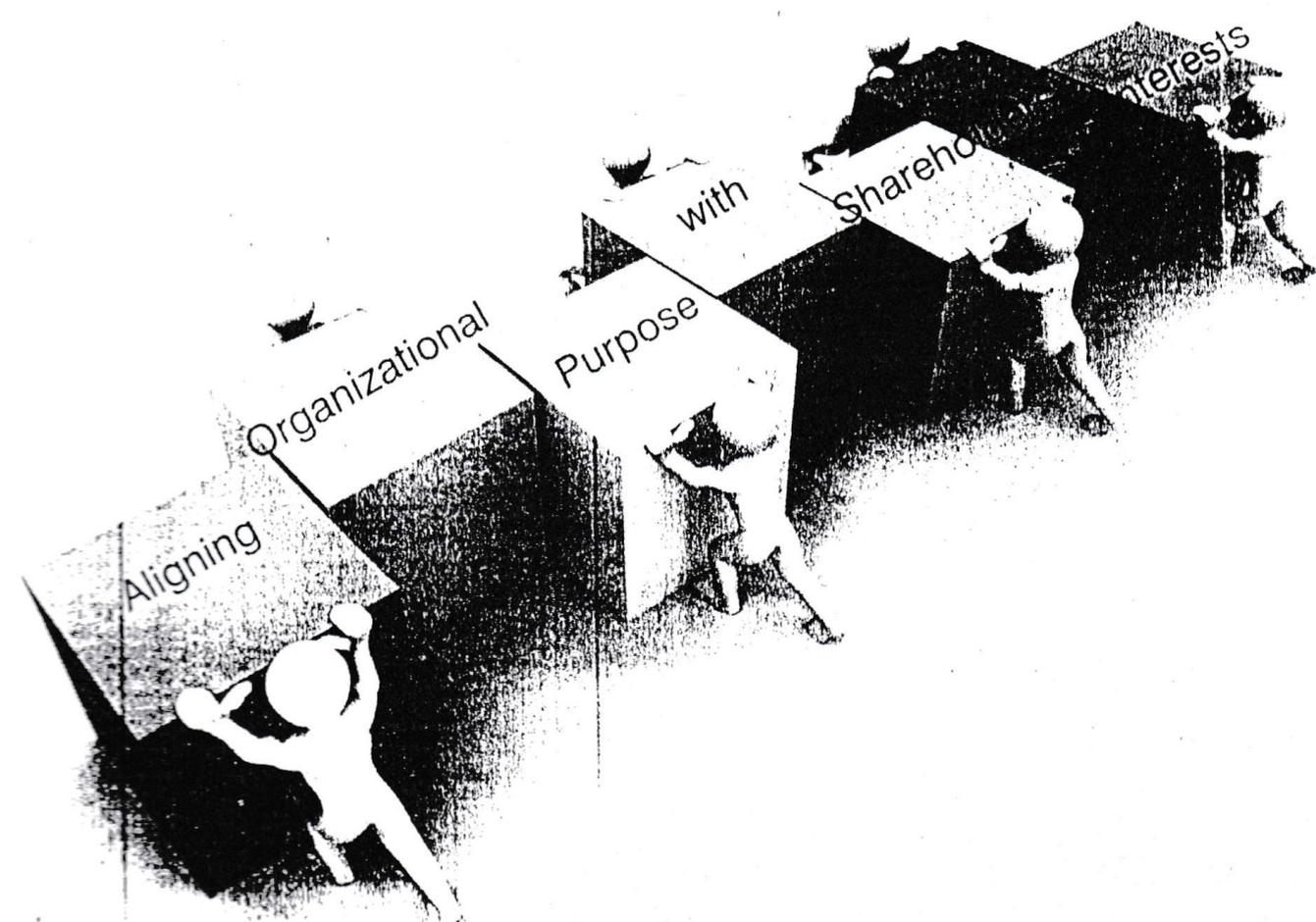




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Impact of Corporate Governance on the Performance of Nigerian Deposit Money Banks

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Abstract

Key Words

Corporate Governance Index
Deposit Money Banks
Bank Performance Index
Information Disclosure

This study examined the relationship between corporate governance practices in Nigerian Deposit Money Banks (DMBs) vis-à-vis their financial performances (2002-06). To accomplish this, data were collected through the use of questionnaire administered to Corporate Affairs Managers in twenty-four Deposit Money Banks (DMBs) and from the Central Bank of Nigeria (CBN) annual report and statement of accounts and Nigeria Stock Exchange (NSE) Fact Books. The data was descriptively and quantitatively analysed and the hypotheses tested using Statistical Package for Social Sciences (SPSS). The regression result of our analysis and test indicated a significant relationship and positive correlation between corporate governance and banks' performance. It is therefore recommended, among others, that Deposit Money Banks (DMBs) in conjunction with the regulatory authorities should model various functions performed by banks and factor in all aspect of corporate governance variables as it may concern a highly regulated industry like the banking industry. This will go a long way in the designing of an optimal governance mechanism for the Deposit Money Banks (DMBs) in Nigeria and beyond.

Introduction

It is often said that there is no resting place for an organization or its chief executive, especially in a competitive environment saddled with government interventions. Banking in Nigeria has passed through several legislative and regulatory changes with a view to repositioning, sanitizing, galvanizing and stabilizing the institution (Agundu et al, 2002). These efforts of the regulators specially the Central Bank of Nigeria (CBN) tend towards fraud detection/prevention and other unethical practices, bad debt recovery, corporate reorganization/reconstruction, statutory (mandatory) financial recapitalization and above all, the need to engender good corporate governance.

Corporate Governance (CG) according to Okereke *et al* (2009) is a way of life that moulds and directs the roles, responsibilities and rights of management and Board of Directors (BODs) of organizations / institutions with a view to achieving the corporate objectives of the

organization and capturing the interests of various stakeholders. It provides decorum on the roles, responsibilities and rights of management and BODs and the need to have respect for each other. It involves mainly disclosure, transparency, fairness, equity, and accountability. It is complying with the rules of the 'game'. That is, doing what the law, policy, procedures and methods specified in a very strict manner with the key elements of CG (transparency, accountability, trust, respect, fairness and honesty) at the background.

There is a renewed emphasis by the regulators – Central Bank of Nigeria (CBN), Nigeria Deposit Insurance Corporation (NDIC), Nigeria Stock Exchange (NSE) & Stock and Exchange Commission (SEC) on the need to improve the corporate governance of the Deposit Money Banks (DMBs) because of the exigency to re-examine the capacity building following the consolidation of the banking sector in 2004. Banks' distress and failure have been attributed to poor or lack of corporate governance. Vanguard of 19 November 2007 report indicated that, "the distress and eventual collapse of these banks was occasioned by factors relating to corporate governance". A study by the Nigeria Deposit Insurance Corporation (NDIC) in 2003 listed the factors that caused severe distress in banks and accounted 51.1% to issues relating to corporate governance. This has therefore raised a number of issues. It ranges from financial disclosure, market discipline, to capacity building, among others. Corporate governance issues have generated intense debate and discussion worldwide, as witnessed by the Sarbanes-Oxley Act in the US, the New Combined Code on Corporate Governance in the UK, and Clause 49 in India.

Though corporate governance is still at its rudimentary stage in Nigeria, it is essentially aimed at raising ethical standards and restoring accountability and transparency. Other studies have shown that engendering good corporate governance has positive effect on portfolio performance, development mission, and reputation risk as well as capital market development. According to Solomon (2007) "companies should care about corporate governance because it provides access to and lowers cost of capital, improves operational efficiency in terms of risk management and improve the companies' reputation".

The cardinal issues in corporate governance in relation to the Deposit Money Banks (DMBs) in Nigeria resides in the proper management of risks, portfolio as well as ethical, reputation, internal control, professionalism issues etc. Therefore, promoting good corporate governance is crucial to the economic performance of the Deposit Money Banks (DMBs). The extent to which this performance is achieved vis-a-vis corporate governance in this sub-sector demands an investigation and this is the focus of this paper.

Objectives of the Study

This research study has the following objectives:

- To examine the extent of transparency and disclosure of information in the Nigeria deposit money banks
- To determine the relationship between the deposit money banks financial performance and their corporate governance.
- To determine the level of commitment of deposit money banks to corporate governance.
- To ascertain the effectiveness of internal control in deposit money banks.

Literature Review

An attempt is made here to present selected local and international works on corporate governance and firm performance. Black, Jang and Kim (2003), in their study reported

that corporate governance is an important factor in explaining the market value of Korean public companies. They construct a corporate governance index (0 - 100) for 531 of the 560 companies listed on the Korea Stock Exchange, relying primarily on responses to a survey conducted by the Korea Stock Exchange (KSE) during the first half of 2001. They find a strong positive correlation between the overall corporate governance index and firm value, which is robust across OLS, 2SLS and 3SLS regressions, in sub-samples, in alternate specifications of the corporate governance index, and with alternate measures of firm value.

In another study on governance mechanisms and banks which examined the impact of various governance mechanisms on bank capital, performance, and merger returns for bank holding companies. Their results are mixed. For example, both managerial compensation and the level of management entrenchment are significant factors whereas board structures have little impact on all three aspects, especially after controlling for other mechanisms. They found that governance does not play a simple role in regulated industries, like banking (<http://www.fma.org>).

Starks et al (2003) in their work hypothesized that corporate governance structures differ systematically across industries and firms due to difference in the costs and benefits of the monitoring mechanisms. In another study Drobert et al (2003) found a strong positive relationship between the quality of firm-level corporate governance and firm valuation. The effect is also significant from an economic point of view. For example, for the median firm, the point estimate in the regression for Tobin's Q implies that a one standard deviation change in the governance rating results in about a 24% increase in the value of Tobin's Q. Larcker D. F., Richardson S. A. and Tuna I. (2004) in their study on How important is Corporate Governance? found that corporate governance constructs have some association with measures of managerial decision making and firm performance and valuation. From these studies, it is obvious that no comprehensive study on corporate governance and performance has been carried out particularly in the banking sector in Nigeria.

Methodology

The study sampled 24 of the 25 consolidated deposit money banks representing 96% of the population. These banks are as shown in Table-2 of the Appendix. Oral interviews were conducted and questionnaire administered to these banks using the corporate affairs managers as proxies for each of them and it showed a response rate of 71%. This helped to construct the Corporate Governance Index (GOVINDEX). Secondary data were obtained from the CBN annual report and statement of accounts with the Nigerian Stock Exchange fact book both of 2006.

The major variables under study include corporate governance and bank performance in Nigeria and they are operationally defined and measured using qualitative and quantitative methods to ensure the validity of the test statistics. Bank performance is operationally defined and corporate governance measured as in equation-2. Our governance index is constructed based on the index of Black, Jang, and Kim (2003).

We classify the governance index variables into five sub-indices:

- Information Access / Disclosure (sub-index A)
 - Audit Committee and Internal Auditor (sub-index B)
 - Board of Directors (sub-index C)
 - Ownership and Control Structure (sub-index D)
 - Ownership Parity (sub-index E)
-

Each element in each sub-index is constructed to have a value between 0 and 1. To obtain a sub index, we compute a simple sum over the elements of the sub index and divide by the number of 'non-missing' elements by standardizing each sub index to have a value between 0 and 20. We combine the sub indices into an overall corporate governance index to get our principal overall Corporate Governance Index (CGI) constructed as indicated below:

$$CGI = A + B + C + D + E \dots\dots\dots (1)$$

Where

CGI = Corporate Governance Index

A, B, C, D, E, the sub indices (A – E)

The overall corporate governance index is finally computed to have a value between zero and 100, with better-governed banks having higher scores. These were regressed against three of deposit money bank performance index (ROA, ROE and EPS). It is the result from our computed corporate governance index that enhances the inferences we made to validate our hypotheses 1, 2, and 3.

The test statistical model developed is as below:

$$DMBPER_i = a_0 + a_1INFOAC_i + a_2AUDITCO_i + a_3BOARDST_i + a_4OWNERCO_i + e_i \dots\dots(2)$$

Where

DMBPER = Deposit Money Bank Performance Indices with the following variables

$$ROA = \text{Return on Asset Ratio} = \frac{\text{Net Income}}{\text{Average Total Asset}}$$

$$ROE = \text{Capital Adequacy Ratio} = \frac{\text{Net Income}}{\text{Equity}}$$

$$EPS = \text{Earnings / Share Ratio} = \frac{\text{Net Earnings}}{\text{Number of Shares}}$$

a_0 = Y – intercept of the regression Equation

$a_1 - a_4$ = the slope of the regression equation

INFOAC = Information Access

AUDITCO = Audit Committee

BOARDST = Board Structure

OWNERCO = Ownership Concentration

e_i = the error terms

The study adopted the qualitative and quantitative methods of analysis using coefficient of correlation, coefficient of determination and any significant relationship and applied SPSS statistical tool.

Data Presentation, Analysis and Interpretation

Data is presented in Table-1 to Table-5 while the analyses are shown in Table-6 to Table-12 and interpretations of results presented thereafter.

Table-1: Data from Questionnaire Responses on Corporate Governance Indices (CGI)

S. No.	Banks	Info. Access	Audit Comm.	B/ Directors Struct.	Control Struct.	Ownership Parity	CGI Scores	% Age Score
1.	Access bank	5	5	4	5	0	19	86.36
2.	Africbank	4	3	4	3	0	14	63.64
3.	Diamond Bank	5	4	3	4	2	18	81.82
4.	EcoBank	5	4	5	3	0	17	77.27
5.	ETB Bank	4	5	4	4	2	19	86.36
6.	FCMB	4	5	5	4	2	20	90.91
7.	Fidelity Bank	4	5	4	4	2	19	86.36
8.	First Bank	5	4	5	5	2	21	95.45
9.	First Inland Bank	5	4	4	4	0	17	77.27
10.	GTB Bank	5	4	4	4	0	17	77.27
11.	IBTC Bank	4	4	5	4	2	19	86.36
12.	Intercontinental Bank	4	5	4	5	0	18	81.82
13.	NIB Bank	5	5	5	5	0	20	90.91
14.	Oceanic Bank	4	5	4	5	0	18	81.82
15.	Platinum Bank	NA	NA	NA	NA	NA	NA	NA
16.	Skye Bank	3	4	4	4	0	15	68.18
17.	Spring Bank	3	5	4	4	0	16	72.73
18.	Stanbic Bank	3	4	5	4	0	16	72.73
19.	Standard Chartered Bank	4	5	5	3	2	19	86.36
20.	Sterling Bank	4	5	5	4	0	18	81.82
21.	UBA	5	5	5	4	2	21	95.45
22.	Union Bank	5	5	4	4	2	20	90.91
23.	Unity Bank	4	4	5	3	2	18	81.82
24.	Wema Bank	4	5	4	5	0	18	81.82
25.	Zenith Bank	5	5	4	5	0	19	86.36

Source: Survey 2008

The table above represents the questionnaire responses and was constructed based on the Index of Black, Jang, and Kim (2003) for Corporate Governance Index (CGI).

Table-2: Governance Variables in Percentages

S. No.	Banks	Control Structure	Info. Access	Audit Comm. %	B/Directors Struct %
1.	Access bank	100	100	100	80
2.	Africbank	60	80	60	80
3.	Diamond Bank	80	100	80	60
4.	EcoBank	60	100	80	100
5.	ETB Bank	80	80	100	80
6.	FCMB	80	80	100	100
7.	Fidelity Bank	80	80	100	80
8.	First Bank	100	100	80	100
9.	First Inland Bank	80	100	80	80
10.	GTB Bank	80	100	80	80
11.	IBTC Bank	80	80	80	100
12.	Intercontinental Bank	100	80	100	80
13.	NIB Bank	100	100	100	100
14.	Oceanic Bank	100	80	100	80
15.	Platinum Bank	NA	NA	NA	NA
16.	Skye Bank	80	60	80	100
17.	Spring Bank	80	60	100	100
18.	Stanbic Bank	80	60	80	100
19.	Standard Chartered Bank	60	80	100	100
20.	Sterling Bank	80	80	100	100
21.	UBA	80	100	100	100
22.	Union Bank	80	100	100	80
23.	Unity Bank	60	80	100	100
24.	Wema Bank	100	800	100	80
25.	Zenith Bank	100	100	100	80

Source: Survey 2008

This table represents the standardize values of the Corporate Governance Index (CGI) in Table-6 and herein represented in percentages based on the index of Black, Jan, and Kim (2003).

Table-3: Deposit Money Banks (DMBs') Governance Index Mean Scores

	Info Access	Audit Comm.	Board Structure	Ownership & Control
Mean	85.8%	91.7%	89.2%	82.5%
Standard Deviation	13.81	11.67	11.76	13.59

Source: Survey 2008 and SPSS Result

The table above represents the mean scores (i.e. the sum total of scores by each bank divided by the total number of banks as in Table-2) and the standard deviation (SPSS result) for each of the Corporate Governance Indices.

Table-4: Performance Indices of Deposit Money Banks

	2002	2003	2004	2005	2006
Capital + Reserve (N1) in Millions	555284.6	391525.0	384880.5	1106946	1424649.9
Net Worth (Equity) in Millions	439620.2	537207.8	686076.6	950551.6	1283146.4
Total Assets (in Millions)	2705749.3	3047856.3	3753277.8	4515177.6	6400783.9
♦ Average Earnings Per Share	36.33	28.67	31.25	17.21	10.53

Sources: CBN Annual Report & Statement of Accounts (2006, 2005).

♦ Derived by Authors from the Nigerian Stock Exchange (NSE) Fact Book (2006, Pg. 106 – 146)-

The table above is an excerpt from the Central Bank of Nigeria (CNB) Annual Report and Statement of Accounts and Nigerian Stock Exchange (NSE) Fact Book on the Performance Indices of the Deposit Money Banks.

Table-5: Performance Ratios

	2002	2003	2004	2005	2006
Return on Assets (ROA)	20.52	12.84	10.25	24.52	22.26
Return on Equity (ROE)	123.31	72.88	56.10	116.45	111.03
Earning Per Share (EPS)	29.30	23.12	25.20	13.88	8.49
Total	173.13	108.84	91.55	154.85	141.78
Average Performance Ratios	57.71	36.28	30.52	51.62	47.26

Source: Survey 2008

This table indicates the performance ratios and average performance ratios based on the values of the performance indices in Table-4 above and in line with the performance ratios formulae adapted from Okereke (2003).

Table-6: Analysis of Corporate Governance Scores

	Corporate Governance Mean Scores	Frequency	Percent	Valid Percent	Cumulative Percent
Valid	63.64	1	4.0	4.2	4.2
	68.18	1	4.0	4.2	8.3
	72.73	2	8.0	8.3	16.7
	77.27	3	12.0	12.5	29.2
	81.82	6	24.0	25.0	54.2
	86.36	6	24.0	25.0	79.2
	90.91	3	12.0	12.5	91.7
	95.45	2	8.0	8.3	100.0
	Total	24	96.0	100.0	
Missing	System	1	4.0		
Total		25	100.0		

Source: SPSS Result

This table represents the SPSS result of governance score data analysed to test our hypothesis three.

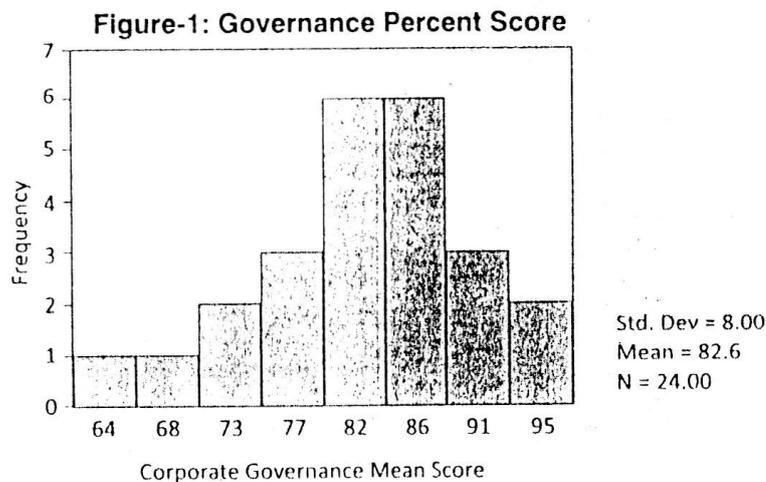


Figure-1 represents the histogram of the analysed data in Table-6.

Table-7: Analysis of Information Access

	CG (Information Access) Mean Scores	Frequency	Percent	Valid Percent	Cumulative Percent
Valid	60.00	3	12.0	12.5	12.5
	80.00	11	44.0	45.8	58.3
	100.00	10	40.0	41.7	100.0
	Total	24	96.0	100.0	
Missing	System	1	4.0		
Total		25	100.0		

Source: SPSS Result

This table represents the SPSS result of information access data analysed to test our hypothesis one.

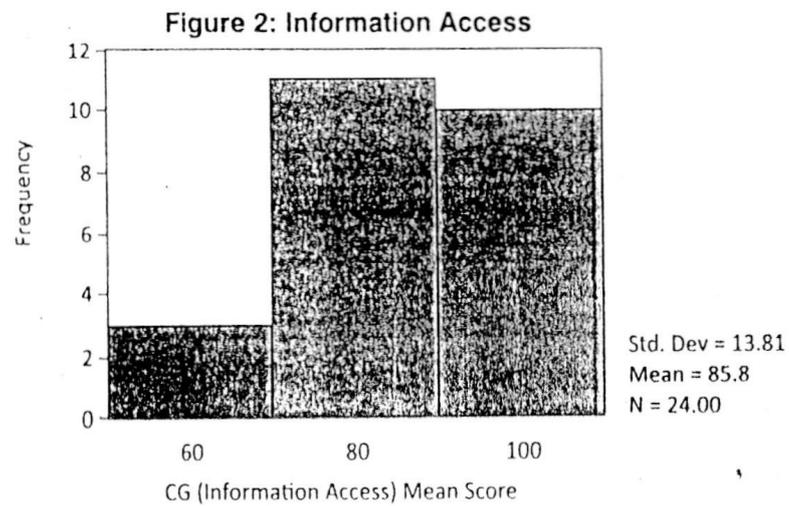


Figure 2 represents the bar chart of the analysed data in Table-7

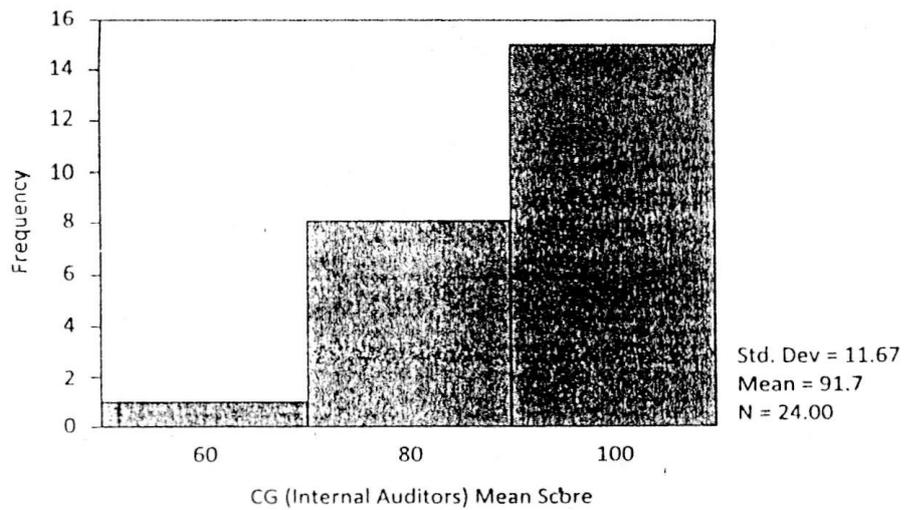
Table-8: Analysis of Internal Audit

	CG (Internal Audit) Mean Scores	Frequency	Percent	Valid Percent	Cumulative Percent
Valid	60.00	1	4.0	4.2	4.2
	80.00	8	32.0	33.3	37.5
	100.00	15	60.0	62.5	100.0
	Total	24	96.0	100.0	
Missing	System	1	4.0		
Total		25	100.0		

Source: SPSS Result

This table represents the SPSS result of internal audit data analysed to test our hypothesis four.

Figure-3: Internal Auditors



This figure represents the bar chart of the analysed data in Table-8

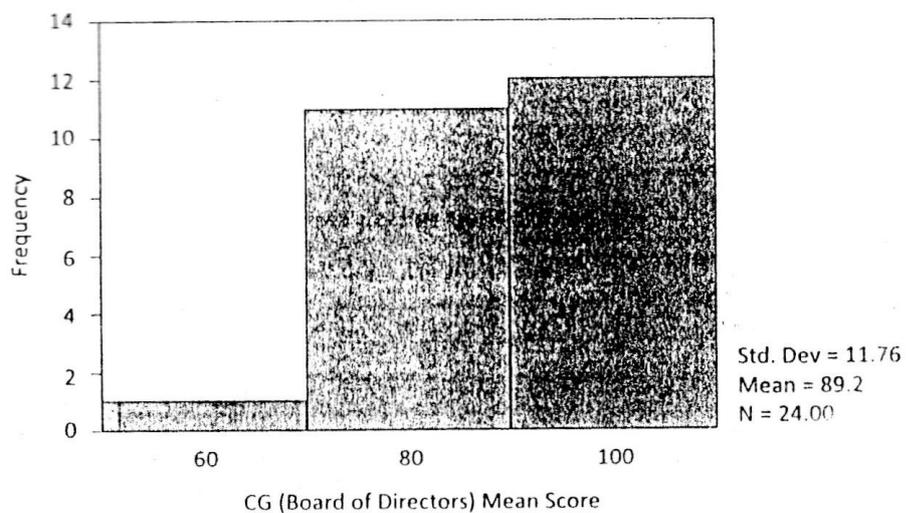
Table-9: Analysis of Board of Directors

	CG (Board of Directors) Mean Scores	Frequency	Percent	Valid Percent	Cumulative Percent
Valid	60.00	1	4.0	4.2	4.2
	80.00	11	44.0	45.8	50.0
	100.00	12	48.0	50.0	100.00
	Total	24	96.0	100.0	
	System	1	4.0		
Total		25	100.0		

Source: SPSS Result

This table represents the SPSS result of board structures data analysed.

Figure-4: Board of Directors



This figure represents the bar chart of the analysed data in Table-9.

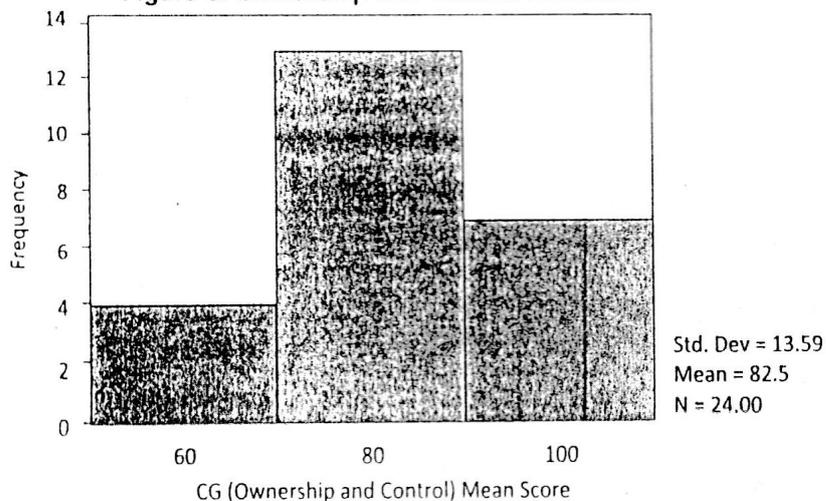
Table-10: Analysis of Ownership Control

	CG (Ownership and Control) Mean Scores	Frequency	Percent	Valid Percent	Cumulative Percent
Valid	60.00	4	16.0	16.7	16.7
	80.00	13	52.0	54.2	70.8
	100.00	7	28.0	29.2	100.0
	Total	24	96.0	100.0	
	System	1	4.0		
Total		25	100.0		

Source: SPSS Result

This table represents the SPSS result of ownership concentration and control data analysed.

Figure-5: Ownership and Control Structure



This figure represents the histogram of the analysed data in Table-10.

Regression Results

Table-11: Model Summary

Model	R	R Square	Adjusted Square	Std. Error of The Estimate
1	.654	.428	.238	9.71897

a. Predictors: (Constant), CGI (d)

This table represents the model summary of our results as was generated by the SPSS for hypothesis two

Table-12: Regression Coefficients

		Unstandardized Coefficients	Std. Error	Standardized Coefficients	T	Sig.
		B		Beta		
1	(Constant)	41.420	4.859		8.524	.003
	CGI (d)	.197	.132	.654	1.499	.231

a. Dependent Variable: PERF

This table represents the regression coefficients as was generated by the SPSS for hypothesis two.

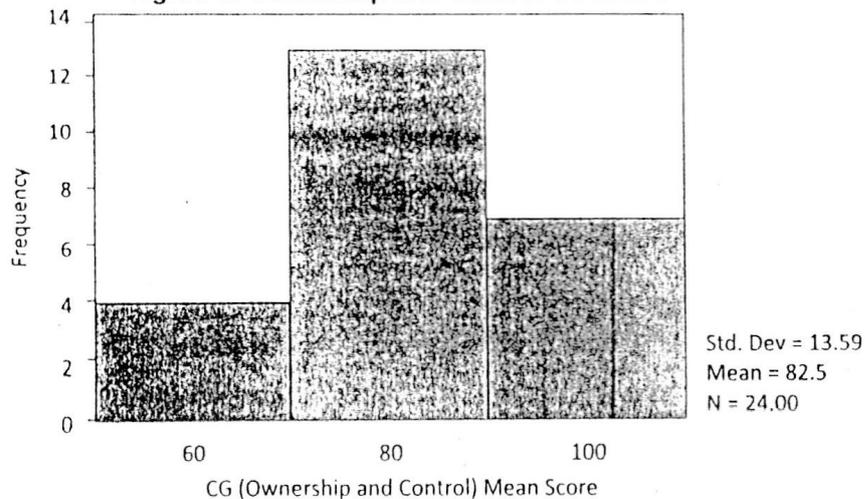
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	100.00	7	28.0	29.2	100.0
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CENTRE FOR CORPORATE GOVERNANCE



INSTITUTE OF PUBLIC ENTERPRISE

OU Campus, Hyderabad – 500007, Andhra Pradesh, India

Corporate Governance (CG) is a system of structural, procedural and cultural safeguards designed to ensure that a company is run in the long-term interests of all of its stakeholders. CG is based on the principles of integrity, fairness, transparency and complying with the laws while conducting the business.

The Centre for Corporate Governance (CCG) has been set up at IPE, which believes that a deep understanding and appreciation of CG-related issues are now essential for all managers, as CG is central to corporate leadership and strategic decisions, social responsibility, various regulatory issues, shareholder value vs. stakeholder value, Board of Directors' role, ethical dilemmas and choices, credibility management, moral issues in insider trading and ownership, setting corporate vision and strategic direction, top-management evaluation and compensation, etc. ONGC has set up a '**Subir Raha Chair of Corporate Governance**' at the CCG.

CCG Objectives

The primary aim of the CCG is to build and disseminate knowledge of CG through its research, publications, seminars, conferences and workshops. It also provides consultancy to government organizations, public and private companies, as well as NGOs in implementing the highest standards of CG. Through its training programs, the CCG enables existing and future directors to better understand the varied aspects of CG, thus making them effective contributors of the board. Its research publications support setting of standards and policy formation by regulatory bodies, professional institutes and industry associations.

CCG Activities

- **Research:** Through its research activity, the CCG generates a vast pool of knowledge on different aspects of CG which would be of interest to academicians, practitioners and policy makers.
- **Training:** The CCG's training programs are aimed at developing knowledge and skills on CG and other board-related matters, to enable directors to be more effective members on the board.
- **Consultancy:** The CCG provides consultancy to government organizations, public and private companies, as well as NGOs in implementing CG procedures and practices at par with the best organizations.
- **Publication:** 'The Indian Journal of Corporate Governance' is a bi-annual refereed journal published by the CCG, to provide a forum for discussion and exchange of views on CG issues by policy makers, practitioners and academicians. The CCG also brings out various articles and working papers on CG issues.
- **Seminars & Conferences:** The CCG regularly organizes seminars, conferences and distinguished lectures to deliberate and discuss the many facets of CG.

Research Assistant: Subir Raha Chair of CG

We invite applications for the position of 'Research Assistant' for the 'Subir Raha Chair of Corporate Governance'. The applicants must possess good research and analytical ability, as well as writing and communication skills. Those pursuing / planning to pursue M Phil / PhD in the area of CG will be preferred. Interested persons may contact:

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Hypotheses Testing and Results Interpretation

The first hypothesis states that: there is no significant level of transparency and disclosure of information by the deposit money Banks in Nigeria. Our governance score has indicated that about three banks have a 60% level of transparency and disclosure of information, about eleven of them have 80% level and ten of them claimed 100% level of transparency and disclosure. The results also indicated that there is a mean score of 85.8% for the entire deposit money banks and also a standard deviation of 13.81. This result rejects the null hypothesis, which implies that there is high level of transparency and disclosure of information in our deposit money banks.

The second hypothesis states that there is no significant relationship between corporate governance and deposit money bank performance. Our regression results from Table-11 showed that the coefficient of correlation (R) is 0.654, which indicates that there is a positive relationship between the corporate governance and performance of the deposit money banks. The coefficient of determination (R^2) of 0.428 (43%) means that about 43% of the total variation in the deposit money banks performance can be explained by the independent variable (corporate governance). From our t-test, we conclude that there is a positive and significant relationship between corporate governance and the performance of the deposit money banks in Nigeria.

Hypothesis three states that there is no significant commitment to corporate governance in Deposit Money Banks' in Nigeria. The hypothesis is tested using the descriptive statistics with the results as shown above in Figure-1. The scores indicated that one bank scored 65%, one bank scored 70%, five banks scored 80%, five banks scored 85%, three banks scored 90% and two banks scored 96%. On the average the banks had a score of 82.58% with a standard deviation of 8.0. This indicates that the banks are committed to corporate governance. Therefore we fail to accept the null hypothesis.

Hypothesis four is stated as: there is no significant effective internal control in the deposit money banks. The result indicated that only four banks have 60% effectiveness, thirteen banks with 80% effectiveness and seven of them with 100% effectiveness. This has shown an average of 82.5% and 13.59 standard deviation effectiveness in the deposit money bank internal control structure. With this result we fail to accept our null hypothesis, meaning that the banks have an effective internal control.

Conclusions

For deposit money banks' transparency and accountability to be meaningful, information disclosed must be comprehensive, relevant and timely, comparable and pass the materiality test. The results of our study affirm these. Hypotheses 1 and 4 have also indicated that there is transparency and effective internal control in the banking system and hypothesis two showed that there is a positive correlation between the corporate governance and the deposit money banks performance.

Given the results of our study, we therefore conclude that the deposit money banks are committed to corporate governance with effective internal control and high level of transparency and disclosure of information. However, the contribution of corporate governance to deposit money banks' performance of about 43% shows that there is still room for improvement.