

Abstract

Asmaa Halmy Abdel Razyk

Corporate Governance characteristics and Earnings Management: An Empirical Study in Egypt

In today's globalized and interconnected world, and due to the consequences of the recent corporate scandals events, economists, the corporate sector, and policymakers worldwide recognize the potential macro-economic, distributional, and long-term consequences of weak corporate governance systems. Egypt started to implement new economic reform programs to gain the trust of the international community and the foreign direct investment. Corporate governance has been perceived by emerging and developing countries as a key source of regulatory framework. This research intends to provide better understanding of the effect of corporate governance on earnings management practices in emerging markets. Specifically, this research investigates the influence of corporate governance characteristics (Board Composition Ownership Structure, and the Presence of Audit Committees) after controlling firm specific characteristics (Firm Size Firm Growth Financial Leverage and Survival effect) on earnings management by Egyptian listed companies. Modified Jones model was used to estimate the absolute discretionary accruals as a proxy for earnings management. The modified Jones model provides the most powerful model in estimating earnings management (Dechow et al., 1995 Guay et al., 1996 and Stolowy et al., 2004). Data was collected for the top 50 most active-traded non-financial companies listed in the Egyptian Stock Exchange over the period 2004-2013, employing an OLS regression model. Results show that corporate governance characteristics relating to the CEO duality and Institutional ownership are good mechanisms for constraining earnings management (Absolute Discretionary Accruals), while size of the board and CEO duality are good mechanisms for constraining positive earnings management and institutional ownership are good mechanisms for constraining negative earnings management. Also, results relating to firm specific characteristics showed that the Firm Size negatively affect both absolute discretionary accruals and positive discretionary accruals (income increasing), while Leverage has only a positive impact on earnings management (Absolute Discretionary Accruals). Moreover, other independent variables such as Board Independence, Size of the Board, Board Meeting, Managerial Ownership and Blockholders Ownership have insignificant effect on the absolute discretionary accruals. Also, other variables relating to firm specific characteristics such as firm growth, and Survival effect have insignificant effect on the absolute discretionary accruals of the top 50 most active firms in the Egyptian stock exchange over the period of the study. It has also been concluded that corporate governance characteristics are likely to limit earnings management in an emerging country such as Egypt if the Egyptian regulatory authorities revise and improve the code of corporate governance characteristics such as board independence and CEO duality.