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Does corporate governance and balance sheet features influence the financial policy of cooperatives in south west Ethiopia? A partial least square structural equation model (PLS SEM)

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Abstract

Efficient financial policy lowers the business risk, improve the net present value of the firm's investment projects and maximize the shareholders' value. However, the effect still not studied yet in the study area. Therefore, the aim of this study is to empirically examine the effects of corporate governance and balance sheet features on the financial policy of cooperatives in south west Ethiopia using the PLS SEM model. Three years' data from 2020 to 2022 were collected from 145 cooperatives. The study used managerial characteristics' as the control variables, corporate governance and balance sheet features as the latent variables that affect the dependent variable cooperative financial policy measured both by short term debt and total debt. The study found that corporate governance has significant but negative effect on the financial policy of cooperatives in south west Ethiopia. It was found that balance sheet features are significant and positive effect on the financial policy of cooperatives in south west Ethiopia. Furthermore, managerial characteristics' have positive effect on the financial policy and balance sheet features and no effect on the corporate governance of cooperatives in south west Ethiopia. Thus, the study concludes that all corporate governance, balance sheet features and managerial characteristics' have significant effect on the financial policy of cooperatives in south west Ethiopia. Therefore, the study recommends that in developing up their financial policy, cooperatives need to take into account managerial characteristics', corporate governance, and balance sheet features.

Key words: Cooperatives, corporate governance, managerial characteristics, and balance sheet features and financial policy.

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Chapter One

1. Introduction

One of the most critical aspects of managing a business is the decision on the financial policy. An increasing business typically requires capital that can be funded by a mixture of debt and equity Mangena, M., and Tauringana, V. (2008). Good financial policy may lower business risk, improve the net present value of the firm's investment projects and maximize the shareholders' value (Gitman, 2003). An appropriate financial policy is essential not only to maximize returns but also to enhance an organizational ability to comply with the requirements of the competitive environment (Abor and Biekpe, 2005).

The role of the financial manager would be to find the optimum financing mix that increases shareholder value (Mak& Li, 2001). The variations in the variety of market decisions in the financial policy provide useful insight into the factors driving those decisions. For cooperatives, the option of financial policy is important because the operational cash flow is allocated between creditors and members, leading to disputes between members and managers. Therefore, the assessment of the optimum capital and decision-making on financial resources are critical problems that can have a direct effect on cooperative economic activities and business relationships.

The financial policy of firms' significantly determined by the organizational structure, characterized by the traditional conceptual separation of ownership and control. Due to positions/powers and divergence of interest between the principal (owner) and the agent (manager), there may be some governance issues, called agency problems. These controversies may be resolved to avoid business failures, financial crises, bankruptcy costs, and corporate collapse at large. This separation of ownership and control, along with their conflicting objectives and information asymmetry between the owners and managers, leads to the self-interested behavior by the managers of the company (Coase, 1937; Jensen and Meckling, 1976; Fama and Jensen, 1983).

Corporate governance refers to the mechanisms, processes, procedures, responsibilities and accountabilities designed to reduce the conflict of interest inherent in the corporate form and ensure that shareholder's interests are protected (Fernando, 2011). It is a control and monitoring system in which the board of directors oversees the work of management to maximize shareholder value (Jebran & Chen, 2020). Corporate governance is one of the most important dimensions of ESG (environmental, social and governance) indices, revealing its capacity to ensure legitimacy (Brammer & Pavelin, 2008; Akhtaruzzaman et al., 2021; Buallay, 2019; Miralles-Quirós et al., 2019). Corporate governance aims at facilitating effective monitoring and efficient control of business. Its essence lies in fairness and transparency in operations and enhanced disclosures for protecting the interests of different stakeholders (Arora & Bodhanwala, 2018). Moreover, corporate governance structures are expected to help the firm perform better through quality decision-making (Shivani et al., 2017).

Good corporate governance reduces the information asymmetry between managers and shareholders. It lowers the cost of capital for the firm as the corporate disclosure and transparency enhance its stock market liquidity, ultimately reducing the transaction cost for the firm's stocks (Diamond and Verrecchia, 1991). Corporate governance and financial policy are linked due to the existence of agency problems in the firms, which may be costly for the firm by increasing its cost of capital and ultimately, readjusting or changing the financing mix of the firm (Hail and Leuz, 2006; Francis et al., 2005; Zhu, 2012; Zaid et al., 2020). Hence, based on the above discussion, we argue that corporate governance directly affects the financial policy and may indirectly affect the firms' financing choices by reducing the cost of capital

Since decision-making on financial policy and cooperative finance can have a huge effect on different aspects of the future situation of cooperatives, these decisions are very relevant and have a direct impact on the value of cooperatives and their members. Boards have different attributes, such as board size, meeting and duality (Hassan and Butt, 2009), which contribute to the financing choice for businesses, among others. In addition balance sheet and income statement features such as profitability, size, growth opportunities, and tangibility of assets, non-debt tax shield, volatility, and liquidity affect the financial policy of firms Sinan (2010). It is

therefore, important to analyze whether the corporate governance and balance sheet features can strengthen or weaken the financial policy of cooperatives.

1.2. Statement of the problem

One of the problems faced by cooperatives is their undercapitalization and financial policy (Cook and Illiopoulos, 1998). Investments are too costly to make, due to insufficient financial resources and relatively high capital costs that makes members deprived from profitable opportunities. A number of arguments have been put forward to clarify the capital constraints faced by cooperatives and their adverse effects on the assets of members Bacchiega and De Fraja (1999). The structure of property rights and the disincentives it offers to its members to invest is one of the most important of these. Indeed, traditional cooperatives are wholly dependent on their current members' money to trade, thereby limiting the cooperative's ability to find investment funds from all potential institutions.

Previous models have shown that the cooperative financial policy is less successful than that of investor-owned companies (Bonin et al., 1993). The key reasons for this disparity appear to be factors such as less "tradability" of ownership rights or a fixed capital allocation to the pool of capital of cooperatives. This paper argues that other factors that may explain the less productive financial policy of cooperatives relative to investor owned firms may be limited understanding and applications of cooperative corporate governance and problem on the preparation of financial statements and admit in the preparation of audit report.

In addition, theoretical and empirical studies on the relationship between corporate governance and balance sheet features on firms' financial policy exists however, the majority of these studies were conducted using data from advanced markets. Moreover, majority of the cooperatives in the study area are not audited and they do not prepare financial statements that contradicted with cooperative proclamation No 985/2016 article 50. Even if those cooperatives in the study area prepare financial statements and made audit inspections their effect on the financial policy is not well known and not investigated yet. As a result, nothing is known regarding the effect of corporate governance and balance sheet features on financial policy of cooperatives in south west Ethiopia. In this regard, empirical study to evaluate the effect of

corporate governance and balance sheet features on the financial policy of cooperatives is worthwhile.

Aisha J et,al (2021), is among the study that address the effect of corporate governance on the financial policy using panel data set and applied OLS estimation with the proper tests for the most popular panel data models, fixed and random effect models. Claessens et al. (2002) investigated the relationship between corporate governance and financial policy and found that good corporate governance mechanisms help firms through a better access to financing and a lower cost of capital. Moreover, (Handoo & Sharma, 2014) and (Chechet, Garba, & Odudu, 2013) studied on the effect of firm specific (balance sheet) features on the financial policy and found that balance sheet features are significant effect on the financial performance. Neither of these studies combined corporate governance and balance sheet features to assess the size of their impact on the financial policy of financial institutions, nor did they use latent variables to reflect corporate governance and balance sheet features in a structural equation model (SEM).

In order to determine the effect of corporate governance and balance sheet features on cooperatives financial policy this study uses the partial least squared structural equation model (PLS-SEM), which employs statistical methods from path analysis. According to Nitzl (2016), SEMs provide flexibility for testing such models by enabling the use of numerous predictors and standard variables, the construction of latent (unobservable) variables, the modeling of measurement errors for observed variables, and the testing of mediation and moderation interactions within a single model.

1.3. Objective of the study

1.3.1 General objective

The main objective of the study is to identify the influence of corporate governance and balance sheet features on the financial policy of cooperatives in south west Ethiopia.

1.3.2. Specific objectives

1. To investigate the effect of board size on the financial policy of cooperatives in south west Ethiopia.

2. To assess the effect of board meeting on the financial policy of cooperatives in south west Ethiopia.
3. To analyze the effect of board gender diversity on the financial policy of cooperatives in south west Ethiopia.
4. To identify the effect of asset size on the financial policy of cooperatives in south west Ethiopia.
5. To determine the effect of liquidity on the financial policy of cooperatives in south west Ethiopia.
6. To examine the effect of asset tangibility on the financial policy of cooperatives in south west Ethiopia.
7. To assess the practice of corporate governance and financial policy of cooperatives in south west Ethiopia.

1.4. Research hypothesis

In many quantitative researches, writers use research questions. However, a more formal statement of research employs hypotheses. These hypotheses are assertions about the outcome of the results, and they may be written as alternative hypotheses specifying the exact results to be expected (more or less, higher or lower of something). They also stated in the null form, indicating no expected difference or no relationship between groups on a dependent variable (Creswell, 2009). After reviewing, the theoretical and empirical studies the study identify and formulate the following nine (6) hypotheses and one (1) research question to achieve the objectives.

H1: The board size has significant effect on the financial policy of cooperatives in south west Ethiopia

H2: Board meeting has significant and positive effect on the financial policy of cooperatives in south west Ethiopia

H3: Board gender diversity has significant and positive effect on the financial policy of cooperatives in south west Ethiopia

H4: Asset size has positively related to the financial policy of cooperatives in south west Ethiopia.

H5: Liquidity has a significant positive relationship with the financial policy of cooperatives in south west Ethiopia.

H6: Asset tangibility has significant effect on the financial policy of cooperatives in south west Ethiopia.

Q1. What practice do cooperatives have on the corporate governance and financial policy?

1.5. Significance of the Study

Theoretically, the study contributes to the expanding body of research conducted on cooperatives and their financial policies and adds to the financial literature because it is the first of its type to examine the effect of corporate governance and balance sheet features on the financial policy of cooperatives operating in south west Ethiopia using the new PLS SEM approach. From practical point of view, the result of the study provide useful insights to the cooperatives in south west Ethiopia for setting sound financial policy and revise their internal bylaws. Moreover, the finding of this study gives insight to the zonal and regional cooperative office and federal cooperative agency (FCA) on how the cooperatives act according to the proclamation 985/2016 in the study area.

1.6. Scope of the study

The study delimited its scope only to those cooperatives in south west Ethiopia with the objective of investigating corporate governance and balance sheet features effect on the financial policy. In addition, this study delimited to measure the financial policy proxied by debt of cooperatives ignoring the dividend and investment policy measures. Moreover, the data were collected from the audited financial statements of cooperatives from 2020 to 2022.

1.7. Limitations of the Study

The main objective of the study is to identify the effect of corporate governance and balance sheet features on the financial policy of cooperatives in south west Ethiopia. The financial policy indicators selected for the study were limited to only debt policy however; financial policy is also proxied by, dividend policy and investment policy. The corporate governance related explanatory variables that have been used for this study where: board size, board meeting and board gender diversity and the explanatory variables used for balance sheet

features are asset size, liquidity and asset tangibility. Those variables are not the only variables that affect the financial policy of cooperatives under the study area. On the other hand, probability-sampling method was not applied to select the sample from the population, which reduces the sample bias. Finally, the results of this study are not generalized to other sectors other than cooperatives.

1.8. Organization of the paper

This paper is organized into five chapters. Chapter one deal with the introduction part in which statement of the problem, objective of the study, research hypotheses, significance of the study scope of the study and limitations of the study are discussed. Chapter two introduced the review of literature in which both theoretical as well as empirical studies related to the paper is reviewed. Chapter three deals with the issue of research methodology in which research design, research approach, sample design, sampling technique, sources of data and collection methods and data analysis and presentation methods are discussed. Chapter four is discussed about the result and discussions and the final chapter deals with conclusions of the study findings and policy implications.

Chapter Two

2. Review of related literature

2.1. Introduction

Examining the effect of corporate governance and balance sheet features influence on financial policy of the cooperatives can be supported by both theoretical and empirical studies. Therefore, in this chapter the concept of cooperatives, corporate governance, financial policy and financial policy related theories are going to be discussed. In addition, the results of different empirical studies conducted on the topic were reviewed under this chapter.

2.2. Concepts of cooperative

In a statement on cooperative identity, the International Cooperative Alliance (ICA, 1995) defines a cooperative as “an autonomous association of persons united voluntarily to meet their common economic, social, and cultural needs and aspirations through a jointly-owned and democratically controlled enterprise”. International Labor Organization (ILO, 1978) defines a cooperative as, “an organization of persons, usually of limited means who have voluntarily joined together to achieve a common economic end through the formation of a democratically controlled business organization making equitable contribution to the capital required, and accepting fair share of the risks and benefits of the undertaking”.

Furthermore, cooperative is defined as a user owned and controlled business that distributes benefits on the basis of use (Zeuli and Radel 2004). This definition recognizes three essential features of cooperatives: user ownership, user control, and proportional distribution of benefits. Cooperatives are based on the values of self-help, self-responsibility, democracy, equality, equity and solidarity. In the tradition of their founders, cooperative members believe in the ethical values of honesty, openness, social responsibility and caring for others. The cooperative principles are guidelines by which cooperatives put their values into practice. There are seven internationally recognized cooperative principles (ICA, 1995). These are voluntary and open membership, democratic member control, member economic participation, autonomy and

independence, education, training and information, cooperation among cooperatives and concern for the community.

2.3. Concepts of corporate governance

Governance can be broadly defined as, the system of people and processes that keep an organization on track and through which it makes major decisions. Bello (2012) defined corporate governance as a concept represents the system by which companies are directed and controlled. Corporate Governance is basically concerned with ways in which all parties interested in the wellbeing of the firm (the stakeholders) attempt to ensure that managers and other insiders are always taking appropriate measures or adopt mechanisms that safeguard the interests of the stakeholders. Such measures are necessitated because of the separation of ownership from management, an increasingly vital feature of the modern corporations (Waseem et al., 2011).

Corporate Governance, therefore, refers to the manner in which the power of a corporation is exercised in the stewardship of the firms' total portfolio of assets and resources with the objective of maintaining and increasing shareholder value and satisfaction of other stakeholders in the context of its corporate mission. It is concerned with creating a balance between economic and social goals and between individual and communal goals while encouraging efficient use of resources, accountability in the use of power and stewardship and as far as possible to align the interests of individuals, corporations and society (Chenuos et al., 2014).

2.4. Financial policy

Corporate investment should be financed appropriately in order to achieve the goal of the corporation. The financing policy is one of the important policies that will influence the company's value. Company must determine their financing mix which will impact on the valuation of companies. The preference source of financing for the company is based on pecking order theory. According to this theory, company will utilize internal sources of financing and rather than employing external financing (debt and equity) because it is the cheapest way to raise fund.

Company has two sources of financing such as internal financing (equity) and external financing (debt). Financing investment project through equity is less risky with respect to cash flow commitment. When debt is used as a source of funding the company is obliged to service its debt.

A company with more debt than equity is considered to be highly leveraged company. Company that is highly leveraged may be at risk of bankruptcy if it is unable to service its debt appropriately. From the perspective of shareholders financial leverage is not always bad but it can increase the shareholders' return on investment because of tax advantage associated with debt. Therefore, it is very important to know the amount of leverage being used by a company. Debt ratio is commonly used to determine whether the company is highly leverage or otherwise. It indicates how company finance its asset whether to use debt or common equity. Recent study conducted by Pindado and Torre (2006), L. Mancinelli et al. (2006), Y.C. Tu et al (2007), Cronqvist and Fahlenbrach (2009) Sulaeman (2008) and Nasser (2010) considered debt ratio as their measurement for financing decision.

2.5. Theories of corporate governance and financial policy

The theories of corporate governance and financial policy include the following;

2.5.1. Pecking order Theory: - Pecking order theory proposes debt isn't predefined rather it states that company's presentations distinctive inclination for using internal over external created assets and firms ought to follow a very much indicated request of need as for financing source to limit its information asymmetry costs initially picking held income, than obligation. Also, the hypothesis presume that as firms become monetarily solid and beneficial, the lesser they looks for outer created assets since they would have enough interior assets to help their venture Myers and Majluf (1984).

2.5.2 Modigliani and miller theory: - Modigliani and Miller's hypothesis proposes that the estimation of the firm didn't rely upon the profit strategy or the debt, prompting a circumstance ordinarily alluded to as debt immateriality. The theory shows that under certain key suppositions, an association's worth is unaffected by its financial policy. Capital market is thought to be impeccable in Modigliani and Miller's reality, where insiders and untouchables have free access to information's; no exchange cost and no tax collection exist; value and

obligation decision become superfluous, and internal and external funds can be consummately subbed (MM, 1958). Moreover, the Modigliani-Miller theorem (M&M) states that the market value of a company is correctly calculated as the present value of its future earnings and its underlying assets, and is independent of its financial policy. At its most basic level, the theorem argues that, with certain assumptions in place, it is irrelevant whether a company finances its growth by borrowing, by issuing stock shares, or by reinvesting its profits.

2.5.3 Trade-off theory: - Trade off hypothesis proposes that organizations have an ideal debt and they move towards the objective. It further underscored that when the obligation is utilized in debt, firms are confronted with the difficulties of the tax cut and liquidation cost, in this manner the requirement for a compromise between the two. Under compromise hypothesis, the organizations with high development openings ought to acquire less on the grounds that it is bound to lose an incentive in monetary misery. This is on the grounds that the compromise hypothesis predicts safe firms. That is firms with more substantial resources and more available salary to shield ought to have high obligation proportions. While firms with more immaterial resources that the worth will vanish if there should be an occurrence of liquidation, need to depend more on value financing. As far as gainfulness, the compromise hypothesis predicts that more productive firms should mean more obligation serving limit and more available salary to shield; in this way, a higher obligation proportion will be envisioned (Myers 2001).

Moreover, an important purpose of the theory is to explain the fact that corporations usually are financed partly with debt and partly with equity. It states that there is an advantage to financing with debt, the tax benefits of debt and there is a cost of financing with debt, the costs of financial distress including bankruptcy costs of debt and non-bankruptcy costs (e.g. staff leaving, suppliers demanding disadvantageous payment terms, bondholder/stockholder infighting, etc.). The marginal benefit of further increases in debt declines as debt increases, while the marginal cost increases, so that a firm that is optimizing its overall value will focus on this trade-off when choosing how much debt and equity to use for financing.

2.5.4. Agency theory:- Agency hypothesis expresses that ideal debt policy can be practiced through the minimization of the office cost by expanding the responsibility for chiefs in the firm or taking more obligation with the end goal of controlling the inclination of directors for over the

top advantage utilizations Jensen and Meckling (1976). Agency theory is a concept used to explain the important relationships between principals and their relative agent. In the most basic sense, the principal is someone who heavily relies on an agent to execute specific financial decisions and transactions that can result in fluctuating outcomes.

2.5.5. Resource dependency theory

The theory postulates that the board of a firm is critical because it provides resources to the managers who in turn utilize them to achieve organizational objectives (Hillman & Dalziel, 2003). The theory recommends the board to provide support to the executives, finance, human, and intangible properties. Board members with expertise and professional should provide training and mentoring to executives to help them improve their skills and performance. Board members can also connect the organization with their personal networks, bringing in vital resources. According to the theory, CEOs should be permitted to make the majority of the firm's decisions, with some being presented to the board for approval. In the case of the banking industry, stakeholder theory consists of satisfying depositors, owners, and other relevant stakeholders based on an effective governance structure that enhances trust and transparency (Vicente-Ramos et al., 2020).

2.6. Empirical literature review and hypothesis development

2.6.1 Corporate governance and financial policy

The decision on the debt structure is critical since a company's profitability is directly influenced by such a decision (Kajanathan, 2012). One of the main elements of the company's financial plan is the efficient collection and use of resources, according to Velnampy & Aloy Niresh (2012). Colombage (2007) notes that debt effectiveness is supported by the presence of a well-developed capital market, financial intermediary, corporate governance and legal security provided by a government. According to Velnampy (2006), "a business organization's financial condition will depend on the resources it owns and the obligations it has to meet." Furthermore, Claessens et al. (2002) argue that effective corporate governance structures benefit companies by easier access to finance and lower capital costs. Corporate governance features that influence the debt policy are the following;

Board size: - Board size is significant determinant of the debt policy of firms. The theory of resource dependence indicates that increased board size will support the organization by supplying the external community with a network and ensuring a wider resource base (Pfeffer and Salancik, 1978; Pearce and Zahra, 1992). Similarly, Berger et al. (1995), claim that, relative to small boards, larger boards seek lower levels of debt. Ciftci et al. (2019), Jackling and 2019 investigated the impact of corporate governance practices on insurance companies' in Nepal and found that large board can improve board independence and diversity, resulting in improved firm performance. Moreover, Schillemans and Bjurstrøm (2020) conducted a study on the impact of corporate governance on the performance of insurance companies, and discovered that board size has a beneficial impact.

Moreover, Saad (2010) conducted a study to investigate the effect of corporate governance on capital structure among public listed companies in Malaysia. This study found that there was a significant positive relationship between board size and debt to equity ratio. The results of Wen et al. (2002), Abor (2007) and Graham (2011) also found there was a positive relationship between board size and debt ratio. They assumed that firms with large board size were more efficient since they would use high debt in order to enhance the firm's value and large board size will contribute to a better decision making due to the knowledge and skill as well as different perspectives of views among the board of directors, hence will make better investment decision. Based on the above arguments, board size is expected to have an impact on policies formulation. For this study it is hypothesized that;

H1: A larger board is strongly linked to financial policy.

Board meeting: - The concept of meeting in corporate governance refers to the frequency of time that the boards meet in a year. Board meetings should be structured to deal quickly with routine financial and operating reports and leave adequate discussion time for strategic issues boards should regularly meet in executive session without management present to discuss matters that may be particularly sensitive regarding management. Equally, a greater frequency of board meetings will lead to a higher quality of management oversight and thus have a positive effect on corporate performance (Vafeas 1999; Ntim, 2009). It has also been argued that daily meetings provide more time for directors to confer, set priorities and review management results (Vafeas 1999). This will allow managers to stay aware and educated about key developments

within the organization and thereby put them in a stronger position to tackle emerging critical issues in a timely manner (Mangena and Tauringana, 2008). This finding was confirmed by Achchuthan et al. (2013), who analyzed the substantial mean gap between corporate governance practices in the financial policy and suggested implementing corporate governance practices towards the debt of the listed manufacturing companies. Therefore, the board meeting hypothesis is;

H2: The frequency of board meeting has significant relationship with the financial policy.

Board gender diversity: - As a gender-diverse committee lowers the asymmetry of information due to higher quality profits, increased accountability, and enhanced public information provision. A gender balanced board has a similar impact on agency issues than a high leverage, as women in the boardroom contribute to greater oversight and thereby reduce agency costs. The influence of a gender-diverse board is also lower for high-debt businesses and higher for low-debt firms. This assertion is rooted in the fact that debt financing and a board that is gender diverse can serve as replacements. Arun et al. (2015) results from the United Kingdom support this reasoning as they provide proof of disparities between high-level debt and low-level debt firms with regard to the impact of a gender-diverse board on earnings management. Their findings indicate that female directors and independent directors have a positive impact on low-level debt firms. Moreover, Zaid et al. (2020) found that board gender diversity has significant effect on the financial policy of firms. Consequently, the hypothesis about the board gender diversity is;

H3: Board gender diversity has significant and positive effect on the financial policy of cooperative

2.6.2 Balance sheet features and financial policy

Balance sheet is a financial statement that reports a company's assets, liabilities, and shareholders' equity. Moreover, balance sheet provides an overview of the state of a company's finance at a moment in time. According to Handoo & Sharma (2014) and Chechet, Garba, & Odudu (2013) balance sheet features impact the debt policy of firms. The paper includes the following explanatory variables as the features of balance sheet that influence the financing policy of cooperatives.

Asset size: - Most of the empirical studies such as, Psillaki and Daskalakis (2009), Mac, Bhaird and Lucey (2010), Daskalakis et al., examined that the relationship between debt and asset size would appear to be positive. The same relationship was concluded by Aybar-Arias et al. (2012), also between the size and speed of debt change. Yazdanfar and Ohman (2016) found the same positive association between asset sizes and long and short term debt. A positive relationship between asset size and long term debt was demonstrated by Cassar and Holmes (2003). Benkraiem and Calin (2013), however, reached the same conclusion about the long-term debt relationship, but a negative relationship between short-term leverage and size was inferred.

Sulong (2009) argued that larger companies have better growth opportunities and access to financing opportunities, less information asymmetry due to availability of information, wider share spread and ownership profile. Pandey (2002) reported that firm size had a positive relationship with debt ratio in Malaysia due to the fact that large firms had lower bankruptcy risk and transaction cost. Moreover, Abebe Z and Ali A (2022) found asset size has significant and positive effect on the financial policy of commercial banks in the emerging market. The hypothesis concerning asset size, therefore, is;

H4: Asset size has significant effect on the financial policy

Liquidity: - Liquidity is considered as the major factor that can affect the financial policy of firms. Majority of the empirical evidences argue that liquidity and financial policy are positively related. Mateev et al. (2013) showed that maintaining higher liquidity levels is fundamentally dependent on long-term debt to finance growth. Again, the association of debt ratio with liquidity is positive according to trade-off theory, because high liquidity firms can pay short-term liabilities on time. Fama and French (2002) found that liquidity has a positive relationship with financial policy. It states that high-liquidity companies should opt for debt as a major contributor to the capital structure, as the company can easily pay off the debt. A number of researchers have recommended that highly liquid companies should use funds generated internally that omits the fixed payment of interest (Deesomsak et al., 2004; Mazur, 2007; Viviani, 2008). Abebe Z and Ali A (2022) also found positive relationship between liquidity and financial policy. The hypothesis concerning liquidity, therefore, is;

H5: Liquidity has a significant positive relationship with the financial policy.

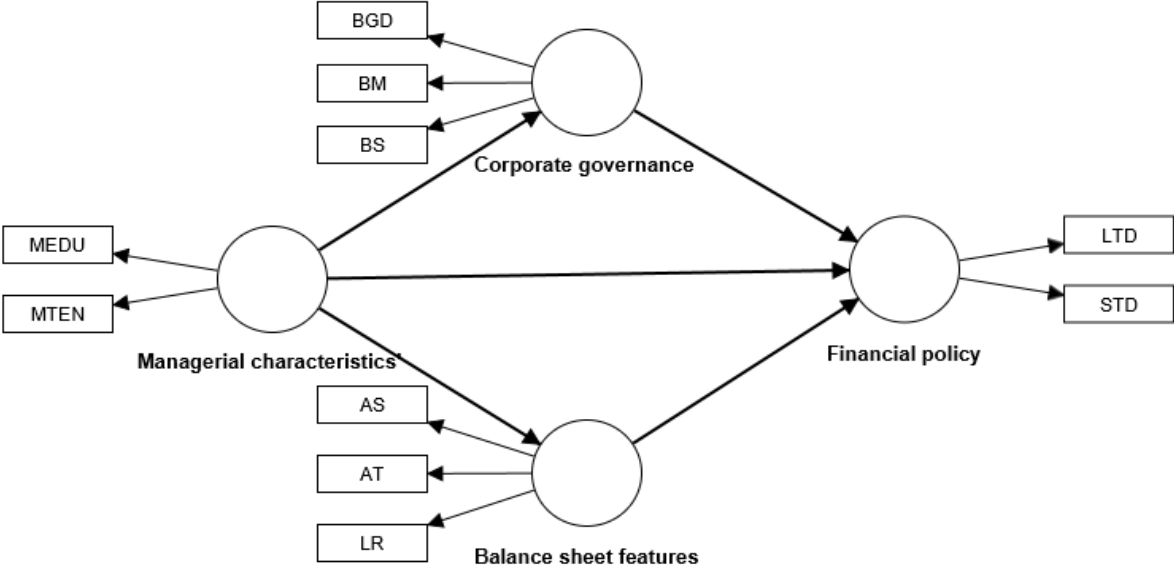
Asset tangibility: - In the form of the tradeoff theory, free cash flow theory and pecking order theory, the shift in asset structure/tangibility would alter the long-term debt ratio. This study assumes that increasing asset structures/tangibility will reduce the use of debt for mature firms, because these firms tend to use internal funds, while growing firms prefer to use debt to finance investors. There is a positive tangibility-debt ratio relationship that is predicted by the theory of trade-offs. The explanation behind the positive relationship is that a business with a large number of fixed assets can easily collect the debt at lower rates due to the collateral value of those fixed assets (tangibility) Berger and Udell (1990). In today's changing world, asymmetric information exists where firms with higher fixed assets can easily obtain debt because it is highly acceptable as a security for creditors. Thus, the asset tangibility hypothesis is;

H6: Asset tangibility has significant effect on the financial policy.

2.6.3. Conceptual frame work

The link between the study's dependent and independent variables is depicted in Figure 1 below. The dependent variable used is financial policy measured both by long term debt (LTD) and short term debt (STD). Furthermore, board size (BS), board meeting (BM) and board gender diversity (BGD), and asset size (AS), liquidity (LIQ) and asset tangibility (AT) are utilized as latent variables to determine corporate governance and balance sheet features respectively. The figure also depicts the relationship between the financial policy of cooperatives and its corporate governance, balance sheet features and managerial characteristics.

Figure1. Conceptual frame work



Sources: Owen design 2023 from SMRT PLS

Chapter Three

3. Research Methodology

3.1. Research design and approach

3.1.1. Research design

The foremost purpose of this study is to identify the effect of corporate governance and balance sheet features on the financial policy of cooperatives. To achieve this objective, explanatory research design were employed to identify and evaluate the cause and effect relationship between the different variables under considerations. In addition, descriptive survey research design would also be used because the questionnaires, interviews and focus group discussions (FGD) were distributed and designed to the board of directors.

3.1.2. Research approach

There are three major categories of research approaches. These are qualitative, quantitative and mixed research approaches. Qualitative research is an approach for exploring and understanding the meaning individuals or groups ascribe to a social or human problem. Quantitative research is an approach for testing objective theories by examining the relationship among variables. These variables, in turn, can be measured, typically on instruments, so that numbered data can be analyzed using statistical procedures. Mixed research approach is an approach to inquiry involving collecting both quantitative and qualitative data, integrating the two forms of data, and using distinct designs that may involve philosophical assumptions and theoretical frameworks. The research approach that was employed in this study is mixed approach.

3.1.3. Source of data and collection methods

Both primary and secondary data were used to conduct the research. The secondary sources of data were collected from audited financial statements of sampled cooperatives between the years (2020-2022). The required secondary data for the study were collected from zone cooperative office. The boards of director were selected to fill the questionnaires because they are in a better position to have all information related to corporate governance of cooperatives. Moreover, the

interviews were also developed to the board of directors to assess the practice of cooperatives on the corporate governance and focus group discussions were carried out again to investigate the practices of cooperatives on the financial policy.

3.2. Population of the study and sampling design

3.2.1. Population of the study

The main purpose of the study is to identify the effect of corporate governance and balance sheet features on the financial policy of cooperatives in south west Ethiopia. According to the Bench Sheko, Sheka and West Omo zones cooperative offices currently there are **673** primary cooperatives serving the cooperative members and the society a whole. The target populations of the study were primary cooperatives that are found in Bench Sheko, Sheka and West Omo zones.

3.2.2. Sampling design

The sample was drawn from the primary cooperatives operating in Bench Sheko, Sheka and Majeing zones. Pilot survey has been made from each wordas and from the total of 673 primary cooperatives the researchers purposively select **145** primary cooperatives that are expected to be used as representatives. The benchmark that used to select primary cooperatives purposively is the availability of three consecutive year financial reports. This implies primary cooperatives that prepared and hold financial statements of the year between 2020 and 2022 were selected as a sample. Moreover, purposive sampling was used because the use of purposive sampling enables the researcher to generate meaningful insights that help to gain a deeper understanding of the research phenomena by selecting the most informative participants that is satisfactory to its specific needs. The selected cooperatives are presented in the table below from each zone respectively.

Table 1: Sample selection of cooperatives

Zones	Total cooperatives	Audited cooperatives
Bench Sheko zone	353	95
Sheka zone	240	25
West Omo zone	80	25
Total	673	145

Source: Zone cooperative office

3.3. Structural equation modeling

According to Bentler and Huang (2014), Bisbe and Malagueo (2015), Hair, Sarstedt, Pieper, Ringle, and Mena (2012), and Nitzl (2016), SEMs provide flexibility for testing such models by enabling the use of multiple predictors and criterion variables, the construction of latent (unobservable) variables, modeling measurement errors for observed variables, and testing mediation and moderation relationships in a single model. All reflected indicators are covered by SEM in a single construct.

The two types of SEM employed in research are partial least squares structural equation modeling (PLS-SEM) and covariance-based structural equation modeling (CB-SEM). PLS-SEM has become more popular than CB-SEM due to theoretical and methodological concerns (Hair, Sarstedt, Ringle, & Mena, 2012; Ringle, Wende, & Becker, 2015). In accordance with Kumar and Sujit (2018), PLS-SEM effectively explains variance that predicts construct relationships, and this approach places more emphasis on maximizing the explained variance of endogenous latent variables than reproducing the theoretical covariance matrix. When dealing with extremely complex data, the PLS-SEM methodology comes in quite handy. Through composites, which are precise linear combinations of the indicators given to the latent variables, this methodology estimates latent variables (Nitzl, 2016).

In light of this, the effect of corporate governance and balance sheet features on financial policy of cooperatives in south west Ethiopia was investigated using the partial least-squares structural equation modeling (PLS-SEM) methodology. The PLS-SEM approach was chosen based on the idea that the corporate governance, balance sheet features, and financial policy are frequently latent and cannot be detected immediately because, using ratios, financial policy cannot be quantified directly until more than one financial policy proxy is utilized. On the other hand, multiple variables are used to measure corporate governance and balance sheet features. Financial policy, corporate governance, and balance sheet features are all latent variables. In order to use PLS-SEM, Smart-PLS software was employed since this method successfully manages nonlinear interactions.

3.4. Variables and measures

Long term debt (LTD) and short term debt (STD) were used as the dependent variable to measure the financial policy, following previous studies (Brailsford et al., 2002; Roshan, 2009). Corporate governance embodied with board size, board meeting and board gender diversity. Similarly, balance sheet features embodied with asset size, liquidity, and asset tangibility of cooperatives were used again as the explanatory variables that can affect the cooperative financial policy. Moreover, managers' tenure and managers' education level as the moderating variables that affect the financial policy of cooperatives. The study variables symbols and measurements are discussed in the table below.

Table 2: Dependent and independent variables

Variables	Observed variable	Proxy
Dependent variable		
	Long term debt	Long term debt/ Total assets of cooperatives
	Short term debt	Short term debt to total asset
Corporate governance		
	Board size	Number of boards in cooperatives
	Board meeting frequency	Number of meetings per year held by the board of directors in cooperatives
	Board gender diversity	Dummy 1 if there is gender diversity 0 other wise

Balance sheet features	Asset size	Natural log of total assets of cooperatives
	Liquidity	Current assets/ current liabilities
	Asset tangibility	Fixed assets/ total assets
Moderating variables		
	Managers tenure	Number of years managers has in cooperatives
	Managers education level	The education level of managers in cooperatives

Source: Own design 2023

Chapter Four

4. Result and discussions

4.1. Descriptive statistics

The mean value of long term debt among cooperatives in south west Ethiopia is 30.3% with the standard deviation of 6.7%. The minimum and maximum value of long term debt of cooperatives in south west Ethiopia is 16% and 68% respectively. The mean value of short term debt of cooperatives in south West Ethiopia is 23% with the standard deviation of 5.2%. The minimum and maximum value of short term debt of cooperatives in south west Ethiopia is 21.2% and 52.4% respectively. The mean value of asset size of cooperatives in south west Ethiopia is 4.052 with the standard deviation of 1.235. The minimum and maximum value of asset size of cooperatives in south west Ethiopia is 6.97 and 2.22 respectively. The mean value of liquidity of cooperatives in south west Ethiopia is 31.8% with the standard deviation of 12.2%. The minimum and maximum value of liquidity of cooperatives in south west Ethiopia is 5% and 97% respectively. The average value of asset tangibility of cooperatives is 29.2% with the standard deviation of 7.2%. The minimum and maximum value of asset tangibility of cooperatives in south west Ethiopia is 2.1% and 84% respectively.

The average cooperative board size (BS) was 9, with a standard deviation of 2 for cooperatives, the minimum and maximum board sizes were 7 and 11, respectively. The average cooperative board meeting is 16 times a year, with 6 times the standard deviation. The minimum and maximum cooperative board meeting is 12 and 24 times a year, respectively. In cooperatives, the board gender diversity of the board is 45.5% with the standard deviation of 49.8%. The board gender diversity of cooperatives for the minimum and maximum is 19% and 28%, respectively. The average educational level of cooperative managers is grade 10 with the standard deviation of grade 8. The minimum and maximum value of managers' education is 10th grade and 12th grade respectively. Finally, the average value of cooperatives managers' tenure is 5.179 with the standard deviation of 1.337. The minimum and maximum value of managers' tenure in cooperatives is 3 and 6 respectively.

Table 3. Descriptive statistics

	Mean	Stand deviation	Minimum	Maximum
LTD	0.303	0.067	0.160	0.680
STD	0.230	0.052	0.212	0.524
AS	4.052	1.235	6.97	2.22
LR	0.318	0.122	0.05	0.97
AT	0.292	0.072	0.021	0.84
BS	9	2	7	11
BM	16	6	12	24
BGD	0.455	0.498	0.19	0.28
MEDU	10	8	10	12
MTEN	5.179	1.337	3	6

Sources: SMART PLS result

4.2. PLS- SEM results

As a first step in PLS-SEM, missing data imputation is carried out by stochastic multiple regression imputation algorithm. The latent constructs consist of reflective measurement scale which are interchangeable and must be highly correlated. In the initial assessment of the model, the loadings of all the variable indicators in the constructs are used for scale purification. Any indicator which has less than 0.5 loading is dropped from the model. This means that the indicator is different from the 0.5 and must not be dropped.

4.3. Internal consistency reliability assessment

Traditionally, the “Cronbach’s alpha” is used to measure internal consistency reliability but it tends to provide a conservative measurement in PLS-SEM. According to Hair et al. (2012), prior literature has suggested the use of composite reliability as a replacement. From this backdrop, the study reported the composite reliability in Table 2. The satisfactory range for composite reliability values are 0.60 to 0.70 in exploratory research and 0.70 to 0.90 in more advanced stages of research. As shown in Table 2, the composite reliability score of the entire latent construct are in the range 0.725 to 0.883 indicating that the latent variables are reliable. Since the construct qualify composite reliability test along with the criteria of average variance extracted (AVE) value is greater than 0.5, the latent variables are retained in the model. Again, Table 2 shows the indicator reliability which is basically the squares of the loading. It can be seen that all the indicators reliability values are much larger than the minimum acceptable level of 0.4 and close to the preferred level of 0.7.

Table 4. Reliability and Validity of latent construct

Latent variables	Indicators	Loading	Indicator reliability	T-test	P- va	Composite reliability	Average variance extracted AVE
Financial policy	LTD	0.989	0.742	1.217	0.041	0.741	0.721
	STD	0.781	0.693	1.315	0.031	0.751	0.832
Corporate governance	BS	0.926	0.662	2.311	0.034	0.821	0.693
	BM	0.791	0.814	1.712	0.000	0.725	0.701
	BGD	0.791	0.723	2.343	0.012	0.824	0.762
Balance sheet features	AS	0.772	0.811	0.214	0.032	0.883	0.831
	LIQ	0.871	0.721	1.331	0.047	0.821	0.762
	AT	0.823	0.72	1.421	0.022	0.767	0.741
Managerial characteristics'	MEDU	0.793	0.744	2.462	0.013	0.821	0.732
	MTEN	0.948	0.823	1.215	0.031	0.772	0.781

Source: SMART PLS result

4.4. Convergent validity

According to Wong (2013), it is relevant to check the construct validity of each variable AVE. If all the AVEs are greater than the threshold of 0.5 the convergent validity is confirmed. From Table 2 above, all the AVEs are more than 0.5 so the convergent validity is confirmed.

4.5. Discriminant validity

Hair et al. (2012) as cited in Kumar and Sujit (2018) argued that discriminant validity certifies that a construct measure is empirically distinctive and represents facts of interest that other measures in an SEM do not capture. Table 3 below shows the Fornell–Larcker criterion which suggests that the square root of AVE must be greater than the correlation of the construct with all other constructs in the structural model. Table 3 shows the correlations among latent variables with square root of AVE by each latent variable. It can be seen that each latent variable AVEs is higher than the correlation of the latent variables indicating discriminant validity of the latent variables.

Table 5. Correlation among latent variables

	Balance sheet features	Corporate governance	Financial policy	Managerial characteristics'
Balance sheet features	0.65			
Corporate governance	-0.346	0.545		
Financial policy	0.884	-0.511	0.524	
Managerial characteristics'	0.153	-0.349	0.176	0.648

Sources: SMART PLS result

4.6. Correlation matrix

The correlation matrix is presented to assess the extent of correlation among the variables and examine the likelihood of multi-collinearity among the regressors. It also establishes whether there is a positive or negative relationship between dependent variables and the independent variables. This is vital as it shows whether there is any relationship between the indicators of corporate governance, balance sheet features and financial policy. The result in Table 4 indicates that the extents of correlation among the regressors were minimal and there is no presence of multicollinearity. The result also shows that there is a significantly positive association between all the balance sheet features as well as managerial characteristics' variables and financial policy. However, corporate governance related variables have negatively correlated with the financial policy of cooperatives.

Table 6. Correlation matrix

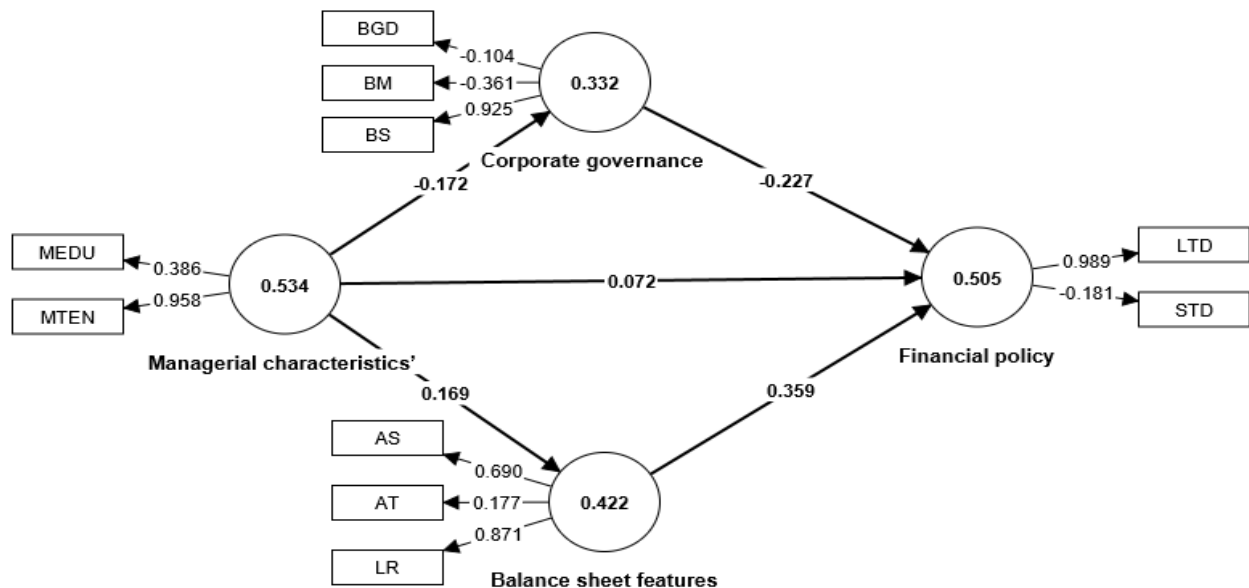
	LTD	STD	AS	LR	AT	BS	BM	BGD	MEDU	MTEN
LTD	1.000									
STD	0.03	1.000								
AS	0.231	-0.08	1.000							
LR	0.37	-0.02	0.250	1.000						
AT	0.05	0.070	-0.025	0.171	1.000					
BS	-0.20	0.030	-0.391	-0.208	-0.065	1.000				
BM	-0.11	-0.03	0.051	0.101	-0.017	0.020	1.000			
BGD	-0.04	0.052	0.053	0.012	0.010	-0.088	0.029	1.000		
MEDU	0.04	0.070	0.063	0.053	0.092	-0.117	-0.003	0.002	1.000	
MTEN	0.07	-0.02	-0.001	-0.064	-0.120	0.135	-0.102	0.022	0.106	0.001

Source: SMART PLS result

4.7. Results of the measurement model of PLS-SEM

To ensure the robustness of the relationship between the latent variables, many schemes are used to estimate the path coefficient of the measurement model. According to Kock (2014) as cited in Kumar and Sujit (2018), this stable method relies directly on the application of exponential smoothing formulas and yield estimates of the actual standard errors that are consistent with those obtained through bootstrapping. This method has proven to yield more precise estimates of the actual standard errors when the linear models are tested using PLS regression and robust path analysis. In Figure 2 however, the significance and the R^2 are presented. The model wise dependent latent variable R^2 showed that both corporate governance and balance sheet features explains 50.5 percent of the financial policy of the cooperatives in south west Ethiopia. On the other hand, the managerial characteristics' variables explain 33.2 percent of corporate governance and 42.2 percent of balance sheet features. This means that the chosen managerial characteristics' variables explain the balance sheet features much better than corporate governance.

Figure 2. Result of linear boot strapping path coefficient



Sources: SMART PLS result

4.8. Discussions of results

This section presents the discussion and analysis of the findings in Figure 2 and Table 5. From the structural path significance in bootstrapping in Table 5, balance sheet features had a statistically significant positive relationship with the financial policy of cooperatives in south west Ethiopia with the coefficient of 0.359 and p- value of 0.000. At a 1% level of significance, balance sheet features has significant and positive relationship with the financial policy of cooperatives, because cooperatives with large balance sheet features (asset size, liquidity and asset tangibility) can practice economies of scale, have better business awareness, and can recruit better managers, and large sizes can allow greater specialization. Moreover, cooperatives having large balance sheet feature specifically asset size can also calculate market power or the level of concentration in the industry by finding external sources of financing for their operations. The outcome of this research is consistent with (Espinosa, Maquieira, & Vieito, 2012) and contrary to Rajan and Zingales (1995) who argue that asymmetry levels are higher for large firms due to the complex knowledge structure.

The discovery of a positive significant relationship demonstrates that cooperatives with a higher balance sheet feature specifically liquidity are capable of meeting their contractual obligations and, thus, resort to debt financing. More importantly, greater liquidity would ensure that cooperatives are able to fulfill their short-term obligations. It can therefore be understood that the effect of liquidity has a greater impact on cooperative financial policy and that the result is consistent with the static trade off theory. Overall, the positive effect of liquidity on financial policy decisions indicates that cooperatives in south-western Ethiopia see liquidity as a guarantee that they can survive and perform their duties when it is difficult for a cooperative to raise funds or in a lower earnings situation, or in periods of very high capital costs. The findings of this report, however, are contrary to the findings of Sheikh and Wang (2012) and Chakrabarti (2019).

Finally, the positive effect of balance sheet features proxied by asset tangibility on cooperatives financial policy is that a business with a large number of fixed assets can easily collect the debt at lower rates due to the collateral value of those fixed assets (tangibility). The observation of a positive significant correlation between the tangibility of assets and the financial policy supports the static trade off theory. Moreover, the results of this research are consistent

with the empirical result of Berger and Udell (1990) since lending to financial institutions is dependent on collateral much of the time.

Again, from Table 5 and Figure 2, corporate governance which was measured by board size, board meeting and board gender diversity showed a statistically significant negative relationship with financial policy of cooperatives with the coefficient of 0.227 and p-value of 0.024. This means that an increase in one unit of corporate governance of cooperatives make weak the financial policy of cooperatives by 22.7percent. The negative effect of corporate governance proxied by board size indicate that the greater number of boards leads to less successful oversight of management because more directors lead to more difficult teamwork and decision-making, and the greater number of boards further decreases corporate debt ratio or increases risky assets. Alves et al. (2015) and Heng et al. (2012) support the finding of this paper, which found that an organization with a higher number of boards decreases its debt ratio and adds risky assets to improve its profitability. This is because wider boards of top executives can have an impact on reducing the efficacy of monitoring activities. For larger boards of executives, these tasks such as planning, communication, and decision-making may be burden and thus make their position less efficient.

In the same way the negative effect of corporate governance on the financial policy of cooperatives indicates that the cooperatives in south west Ethiopia have weak corporate governance that intern affect their financial policy and makes the cooperatives bankrupt. The finding of this study is consistent with (Hail and Leuz, 2006; Francis et al., 2005; Zhu, 2012; Cormier et al., 2010 and Zaid et al., (2020) that supports the concept of weak corporate governance may increase information asymmetry by reducing the corporate disclosure practices and monitoring mechanisms, which ultimately increase agency costs and capital structure choices of the firms.

Table 5, also indicated that the managerial characteristics' related variables which were measured by managers education (MEDU) and managers tenure (MTEN) have significant and positive effect on balance sheet features and negative and insignificant effect on the corporate governance of cooperatives. In that, these variables moderate how balance sheet features affect the financial policy of cooperatives in south west Ethiopia. This infers that cooperatives with high managers education (MEDU) and managers tenure (MTEN) is likely to increase the balance

sheet features of cooperatives in south west Ethiopia and an increase in both managers education and managers tenure does not bring any change on the corporate governance of cooperative in south west Ethiopia.

In relation to the direct relationship between the managerial characteristics' proxies and financial policy of cooperatives is a statistically positive relationship with a coefficient of 0.072 and p- value of 0.041. This means that an increase in both the managers' education and managers' tenure improves the financial policy of cooperatives by 7.2 percent. The significant positive impact of managers' education and managers' tenure on the financial policy of cooperative indicates that highly educated managers prefer to adopt advanced policies that directly influence the financial policy in managerial finance. This study's outcome is consistent with Ahn, Mortara, & Minshall (2014). Moreover, the positive effect of managers' education and managers tenure indicates that highly educated managers and managers with longer tenure allows greater knowledge of the business and market, thereby offering superior monitoring. The outcome is consistent with the theory of experience and Umukoro (2009), which notes that good financial policy will be likely to be used by mangers with long tenure and high education level.

Table 7. Structural path significance in bootstrapping

	Original sample (O)	Sample mean (M)	Standard deviation (STDEV)	T statistics (O/STDEV)	P- v
Balance sheet features -> Financial policy	0.359	0.371	0.059	6.252	0.000
Corporate governance -> Financial policy	-0.227	-0.230	0.100	2.254	0. 24
Managerial characteristics' -> Balance sheet features	0.169	0.156	0.053	2.876	0.004
Managerial characteristics' -> Corporate governance	-0.172	-0.174	0.034	5.094	0.000
Managerial characteristics' -> Financial policy	0.072	-0.015	0.050	0.301	0.041

Source: SMART PLS result

4.9. In-depth interviews result

As stated in chapter three, apart from the structured record review, this study employed in depth interviews with the cooperatives board of directors. The in depth interview was conducted with 30 board of directors 15 from Bench Sheko zone, 10 from Sheka zone and 5 from West omo zone. The interview questions were unstructured and focused on the practices of financial policy of cooperatives relative to investment and dividend policy.

All the interviewees considered financial policy to be an important policy for the cooperatives. Moreover, the discussions demonstrated a broad interdependence of investment, financing and dividend policies exists in cooperatives of south west Ethiopia and decisions about financial policy were not taken in isolation but were considered alongside the investment and financing needs of cooperatives in order to maximize the value of members.

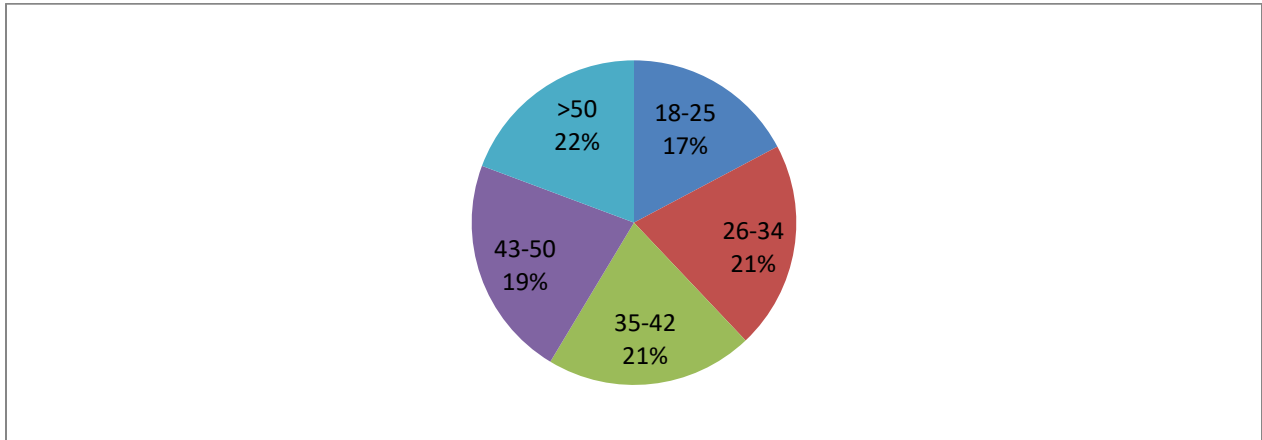
Regarding the financial policy practice of cooperatives the interviewees answered that the cooperatives finance their assets with more equity than debt which is supported by pecking order theory. In response to specific questions about the ratio of debt and equity the interviewee stated that their cooperative did not have determined target ratios and did not finance their asset with similar rate of debt or equity. In addition, the interviewees indicated that financial policy of cooperatives (Debt or equity) fluctuated with the cooperatives change in investment and dividend decisions.

4.10. Questionnaires and focus group discussions result

As stated in chapter three apart from the structured record review and in depth interview this study also employed questionnaires and focus group discussions with the cooperatives board of directors. Both the questionnaires' and focus group discussions focused on the practices of cooperatives on their corporate governance. Through this 145 questionnaires were distributed to the board of directors of cooperatives and focus group discussions were conducted using three (3) groups. Therefore the results of the questionnaires and focus group discussions were discussed below.

Figure 3 below shows that 17% of the respondents were from 18-25 age followed by 21% from 26-34, 21% from 35-42, 21% from 43-50 and 22% above 50 age.

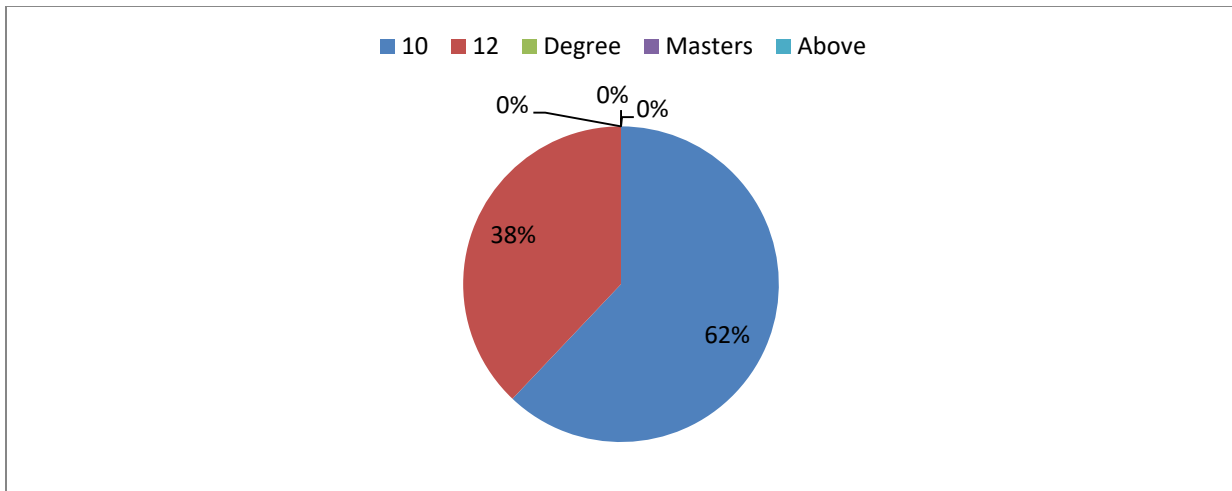
Figure 3. Classification of respondents by age



Source: Owen design 2023

Figure 4 below shows that 62% the respondents were grade 10 and 38% of the respondents were grade 12. The figure also shows that there are no respondents with degree, masters and above education level in cooperatives.

Figure 4. Classification of respondents by education level



Source: Owen design 2023

As a principle all cooperatives should have a board because boards are responsible for making important decisions that affect the cooperative performance and direction, such as setting the

cooperatives overall strategy, selecting and evaluating the performance and ensuring compliance with internal bylaws and cooperative proclamation. From this backdrop, table 8 below shows that all cooperative in south west Ethiopia has their own board. Similarly, the study asked the number of board members and the respondents answered that there are no fixed number of board members but some cooperatives have 5 board members, some have 7 board members, and the other have 9 and 11 board members.

Table 8. Cooperatives corporate governance practices

Questions	Response	Number of respondents	Percentage
Does your cooperative have a board?	Yes	145	100%
	No	0	0
	Total	145	100%

Source: Owen design 2023

Table 9 below shows 66% of the respondents responded that the large number of cooperatives board members did not improve the cooperatives financial policy and 34% of the respondents responded the large number of board members of cooperative improved the financial policy. The result is supported the regression result of the study which states the greater number of boards leads to less successful oversight of management because more directors lead to more difficult teamwork and decision-making, and the greater number of boards further decreases corporate debt ratio or increases risky assets. The result of the questionnaires and regression results are supported by the result of focus group discussions that states the number of board members not that much improve the financial policy of cooperatives in the study area.

Table 9. Cooperatives corporate governance mechanism and their effect on the financial policy

Questions	Response	Number of respondents	Percentage
Do you think that the number of board members improve the financial policy of cooperative?	Yes	50	34% %
	No	95	66%
	Total	145	100%

Source: Owen design 2023

Table 10 below shows 100% of the respondents carried out formal meeting. In addition, the respondents were asked to respond their meeting frequency and responded that there is no similar meeting frequency among cooperatives.

Table 10. Cooperatives corporate governance mechanism and their effect on the financial policy

Questions	Response	Number of respondents	Percentage
Is their formal board meeting in the cooperatives?	Yes	145	100%
	No	0	0
	Total	145	100%

Source: Owen design 2023

As shown in table 11 below 23% of the respondents responded that the board members meeting frequency improves the financial policy of cooperatives in south west Ethiopia. However, 77% of the respondents responded that the members meeting frequency did not improve the financial policy of cooperatives in south west Ethiopia because when the number of board meeting frequency increases there is also an increase in administrative cost of cooperatives that harm their financial policy. The result of the questionnaires and regression results are supported by the result of focus group discussions that states the meeting frequency of cooperative board meeting not that much improves the financial policy of cooperatives in the study area supported by the result of Nimalthasanan (2013).

Table 11. Cooperatives corporate governance mechanism and their effect on the financial policy

Questions	Response	Number of respondents	Percentage
Do you think that board members meeting frequency improve the financial policy of cooperatives?	Yes	33	23%
	No	112	77%
	Total	145	100%

Owen design 2023

As shown in table 12 below 47% of the respondents responded there are female members in the board of cooperatives. However, 68% of the respondents responded that females are not included in the board of cooperatives in south west Ethiopia. Similarly, the respondents were asked on the specific number of females on the board and some cooperatives responded that 0, some

responded 1, the other responded 2, 3, and 4,5,6,7 respectively. In addition, the questionnaires result is supported by the focus group that states majority of the board members are male other than female that contradicted with the cooperative proclamation article 34 sub-article (7) of the Cooperative Proclamation No 985/2016, where there is a potential number of women, at least 30% of any cooperative society management committee is held by female members.

Table 12. Cooperatives corporate governance mechanism and their effect on the financial policy

Questions	Response	Number of respondents	Percentage
In your cooperative are females member of the board?	Yes	47	32%
	No	98	68%
	Total	145	100%

Source: Owen design 2023

5. Conclusions and policy implications

5.1. Conclusions

This paper presents the effect of corporate governance and balance sheet features on the financial policy of cooperatives in south west Ethiopia using the new SMART PLS approach. The study contributes to the strand of works that seek to ascertain empirical evidence in uniquely fixing the financial policy puzzle by focusing on an emerging economy over the period 2020 - 2022.

Using data from the annual report and financial statements of cooperatives, the study constructed PLS SEM to test the effect of corporate governance and balance sheet features on the financial policy of cooperatives. Moreover, the study also used in depth interview, questionnaires and focus group discussions to assess the practices of corporate governance and balance sheet features in cooperatives respectively. The findings found that corporate governance has significant and negative effect on the financial policy of cooperatives in south west Ethiopia. The negative effect of corporate governance on cooperatives financial policy indicted that corporate governance proxied by board size reduces the efficacy of monitoring activities and decreases its debt ratio and adds risky assets. Similarly, the negative effect of corporate governance is because the corporate governance proxied by board meeting frequency increases the administrative cost of cooperative in the study area. The questionnaires and focus group discussions also confirm that the corporate governance not that much improve the financial policy of cooperatives.

Moreover, the study found that balance sheet features have significant and positive effect on the financial policy of cooperatives in south west Ethiopia. The positive effect of balance sheet features (asset size, liquidity and asset tangibility) indicates that cooperatives can practice economies of scale, capable of meeting their contractual obligations and can easily collect the debt at lower rates respectively. Finally, the study results indicated that managerial characteristics proxied by managers education and managers tenure significantly influence the financial policy and balance sheet features and insignificant effect on the corporate governance of cooperatives in south west Ethiopia. Therefore, the study conclude that the financial policy of cooperatives significantly affected by corporate governance, balance sheet features and managerial characteristics factors in south west Ethiopia.

5.2. Policy implications

Based on the finding of the study the following policy implications were given:

- To maximize the cooperatives value and efficient financial policy, cooperatives need to avoid constituting broad board sizes to signal the efficiency of their internal governance to creditors because smaller board sizes actively track cooperative boards. Creditors are therefore concentrating their attention on cooperatives with good corporate governance.
- Board meetings held at least once a month in a financial year, is important for cooperatives to make successful financial policy. However, cooperatives under the study area held more meeting that increase the administrative cost. Therefore, board members in cooperatives have to decrease board meeting.
- Board members need to include more young fresh man in order to benefit from young people's skills. This does not mean that all the board members of cooperatives are all having long tenure rather collaborating board members with short tenure, no experience and long tenure.
- Board members under the study area were male which contradicts the cooperative proclamation No 985/2016, Article 34 sub-article seven (7) where there are a potential number of women, at least 30% of the members of any Cooperative Society board members are women. Therefore, the study advises that cooperatives and cooperative promotion office have to raise awareness of leadership skills by offering short-term tanning to female members and have to put women into leadership. The cooperatives in the field of study and the promotion office, on the other hand, have to observe and control the operation of the cooperative proclamation, precisely Article (34) sub-article (7).
- Large cooperatives calculate market power or the level of concentration in the industry by finding external sources of financing for their operations the study, therefore, recommended that cooperatives must increase their asset size because large cooperatives can practice economies of scale.
- Likewise, liquidity has a major positive impact on the cooperative financial policy. The effect of liquidity can therefore be understood to have a greater influence on the debt funding of cooperatives. Thus, cooperatives have to raise their liquidity during the study period because cooperatives with higher liquidity have the capacity to fulfill their

contractual obligation and, therefore, resort to funding through debt and higher liquidity would ensure that cooperatives will meet their short term duty.

- Asset tangibility has significant positive relationship with the financial policy of cooperatives. Since cooperatives with a large number of fixed assets can easily collect the debt at lower rates due to the collateral value of those fixed assets (tangibility). Cooperatives need to increase their fixed asset percentage because the higher the fixed assets can easily collect the debt at lower rates due to the collateral value of those fixed assets (tangibility).
- Managers' education has a significant and positive relationship with the cooperative financial policy. The study, therefore, suggests that cooperatives equip the managers with up to date industry dynamics and thereby helping cooperatives to make sound financial policy.
- There must be further research on the area by including investment and dividend policy which affect the financial policy that has not been touched by the study.

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