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Impact of Corporate Governance Practices on Financial Distress of Listed Consumer Services Sector Companies in Sri Lanka

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Abstract

The purpose of the study is to examine the impact of corporate governance practices on the financial distress of listed companies in the consumer services sector in Sri Lanka. To assess the level of corporate governance, the current study constructs six dimensions of corporate governance, such as board size, board composition, CEO duality, board meeting, director ownership, and audit committee size. The Altman Z-score is used as a proxy for financial distress. A bigger Z-score indicates smaller risk of financial distress. Using 108 individual observations of Consumer Services firms listed on the Colombo Stock Exchange (CSE) for the period of 2019 to 2021 and by employing fixed effects models, the effect of corporate governance practices on financial distress is evaluated. The results from panel data regressions reveal that firms having a large number of directors on the board have a low likelihood of financial distress. Furthermore, when a chief executive officer serves as the chairman of the board at a company, the company is more likely to experience financial distress. The current study also provides evidence that firm-specific characteristics, such as firm size, leverage, and profitability, could be useful in determining the likelihood of financial distress. The findings are useful to practitioners and regulators interested in understanding the impact of corporate governance practices on financial distress.

Keywords: *Board size, CEO duality, Corporate governance, Financial distress*
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