EFFECTS OF CORPORATE GOVERNANCE ON THE FINANCIAL PERFORMANCE OF COMPANIES LISTED IN THE NAIROBI SECURITIES EXCHANGE

BY

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DECLARATION

This research project is my original work and has not been presented for a degree course in any other university.

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DEDICATION

To my family for their steadfast support and encouragement during the entire period I
undertook this research project.
ACKNOWLEDGEMENTS

I would like to thank the Kenyatta University facilitators who helped take us all through the demanding course modules.

Special thanks go to my Supervisors who tirelessly and wholeheartedly offered me their assistance without reservation.
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<tr>
<th>Acronym</th>
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<td>BODs</td>
<td>Board of Directors</td>
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<td>CEO</td>
<td>Chief Executive Officer</td>
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<td>CG</td>
<td>Corporate Governance</td>
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<td>CMAL</td>
<td>Capital Market Authority Library</td>
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<td>LIFO</td>
<td>Last In First Out</td>
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<td>NSE</td>
<td>Nairobi Stock Exchange</td>
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<td>OECD</td>
<td>Organization for Economic Co-operation and Development</td>
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<tr>
<td>ROA</td>
<td>Return on assets</td>
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<td>ROE</td>
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<td>ROI</td>
<td>Return on Investment</td>
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<td>(SME)</td>
<td>Small and Medium Sized Enterprise</td>
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DEFINITION OF TERMS

Board composition: These are the skills, knowledge, and experience of the board members which enable them perform their duties effectively

Board size: Is a specific number of people who are answerable to shareholders for the safeguarding of their interest through the lawful, informed, efficient, and able administration of the institution

Corporate governance: The manner in which power of a corporation as an entity is exercised in the stewardship of an entity portfolio of assets and resources with the objective of maintaining of increasing shareholder value and while ensuring stakeholder satisfaction within the contents of its mission

Performance: This refers to output results and their outcome obtained from processes, products and services that permit evaluation and comparison relative to goals, standards, past results and other organizations.

Sustainable Responsible Business: This is a form of corporate self-regulation integrated into a business model.

Return on assets: An indicator of how profitable a company is relative to its total assets. ROA gives an idea as to how efficient management is at using its assets to generate earnings. Calculated by dividing a company's annual earnings by its total assets, ROA is displayed as a percentage.

Return on equity: The amount of net income returned as a percentage of shareholders equity. Return on equity measures a corporation's profitability by revealing how much profit a company generates with the money shareholders have invested
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ABSTRACT

In recent times, interest in corporate governance in the African continent has assumed highest propositions. This is probably due to the great push from the developing countries to the African countries to embrace good governance in order to attract foreign investors and to improve shareholders value. The General objective of the study was to investigate the effect of corporate governance on the financial performance of companies listed in the Nairobi stock Exchange whereas the specific objectives were to find out the effects of board size on the financial performance of firms listed in NSE, to establish the effect of board composition on financial performance of firms listed in NSE, to ascertain the effects of ownership concentration on the financial performance of firms listed in NSE and to establish the effect of sustainable responsible business on the financial performance of companies listed in the NSE. This study utilized four main theories i.e. shareholder’s model, stakeholder models, agency theory, management theory, stakeholders theory and stewardship theory. The study used longitudinal research design with the target population being companies listed in the Nairobi stock exchange since the year 2004 after the automation of the systems in the stock market. Secondary Data was collected from the capital markets authority library. Data collected was analyzed using SPSS regression analysis. Findings from the study revealed that the coefficient’s p-values (p=0.001<0.005, p=0.002<0.005 and p=0.004<0.005 for ROA, ROI and ROE respectively) show that the results are statistically significant at 5% significance level. These regression results imply that a unit increase in board size would result in an increase of ROA by 0.231, ROI by 0.219 and ROE by 0.205. From the study, it can be concluded that the board size, ownership concentration, board composition and sustainable responsible business all have a significant effect on the financial performance of companies listed at the NSE. It is evident that corporate governance structure has an influence on financial performance in companies listed in the NSE Kenya. Hence, the study recommends that there is a need to strike a good balance between quality and quantity with regards to board sizes hence board size should be fairly large and not too large that will discourage investors especially shareholders. Further research should be carried More research on individual board structures are needed to assess the effects on its performance. Also future study should look other factors such as shareholders interest, board and CEO compensation to establish its effects on financial performance.
CHAPTER ONE
INTRODUCTION

This chapter introduces the background of the study, statement of the problem, the study objectives, significance of the study and the scope of the study.

1.1 Background of the Study

Boatright, (2002) indicates that financial performance is a subjective measure of how well a firm can use assets from its primary mode of business and generate revenues. This term is also used as a general measure of a firm's overall financial health over a given period of time, and can be used to compare similar firms across the same industry or to compare industries or sectors in aggregation. Measures of financial performance reduce a large amount of information into a convenient form for analysis. No single measure of financial performance is adequate for evaluating a farm business. Evaluation of several financial measures may be more useful in directing the manager to ask the right questions than in providing solutions to the financial problems of the business. Both the magnitude of the measure and its relationship to other measures should be evaluated.

According to Chatterjee (2009), decisions made in developing the balance sheet, cash flow statement, and income statement have important impacts on the financial measures. Some of those decisions include using cost or market values in preparing the balance sheet; determining a specific value for each asset and liability on the balance sheet; including or excluding accrued expenses, deferred taxes, and personal assets and liabilities from the balance sheet; estimating net income on a cash, accrual, or accrual adjusted basis; and deciding if income should be before or after taxes. Each of these decisions affects key relationships in the financial statements and impacts the financial measures used to evaluate financial performance and position.
Ezzamel, and Watson (1997) indicates that the overall performance and position of the business should be evaluated based on a set of criteria that includes liquidity, solvency, profitability, financial efficiency, and repayment capacity. Each of these criteria measures a different aspect of financial performance and/or position. Liquidity indicates the ability of the business to meet financial obligations when they come due. Timely payment of the obligations of the business, including principal and interest on debt without disrupting the normal operation, is an indication the business is liquid.

According to Fabozzi Modigliani (1995), Solvency measures the ability of the firm to pay all debts if the assets of the business are sold. Generally, if the market value of total assets exceeds existing debt obligations against those assets, the business is solvent. Profitability is an indication of the level of income produced by the farm business and is measured in terms of rates of return produced by the labor, management, and capital of the business.

Jensen & Meckling (2006) indicated that financial efficiency measures the degree of efficiency with which labor, management, and capital are used in the business. Efficiency indicates the relationship between inputs and outputs and can be measured in physical or financial terms. Repayment capacity measures the ability of the business to repay existing debt commitments from farm and nonfarm income, and it is closely related to the concept of liquidity. Each of these criteria plays an important role in the analysis of financial performance and position of a business.

1.1.1 Structure of NSE

The Nairobi stock exchange was (NSE) was constituted in 1954 as a voluntary association of stockbrokers registered under societies act until 1991 when it was registered under the companies act when the call and phased out the “the over” trading system in favour of the
floor-based "open outcry system". The Exchange is the Sub-Saharan’s fourth largest bourse. Twenty five brokers are licensed to operate and there are fifty eight Companies listed. The NSE like other emerging markets suffers from lack of liquidity in the market.

The Kenyan government has made several reforms aimed at attracting both local and foreign investment into the market. The Nairobi Stock Exchange is poised to play an increasing role in the Kenyan economy especially in the privatization of state-owned enterprises. The biggest challenge facing the NSE is to increase its turnover ratio. Stockbroker is a regulated professional broker who buys and sells shares and other securities through Stock market on behalf of investors. A transaction on a stock exchange must be made between members of the exchange.

Good governance recommendations are based on the philosophy of promoting market with "minimum interference" (Hamilton, 2004). The corporate governance is based on broad principles with flexibility. The principles cover the board structure, integrity of corporate reporting, shareholders’ rights, executives and directors’ performance and remuneration, and risk management. The recommendations drive the companies to disclose corporate governance information considered as relevant to investors and the disclosure rule requires companies to explain any departure from the best practice principles (Hamilton, 2004).

The best principle emphasizes on promoting effective disclosure of quality and reliable information to investors. Audit services, auditor independence, continuous disclosure and shareholders’ participation are emphasized to ensure the quality of accounting systems and financial information (Maher, & Anderson, 1999) "Corporate Governance effects of firm performance and economic growth)."
Investment in shares seems better investments than other kinds of deposits and bonds. The crucial link in this entire investment circle is the board and the management of the company listed in the stock market. Corporate governance relates to the manner in which the business of the stock market is governed, including setting corporate objectives and risk profile, aligning corporate and behaviors with the expectation that the management will operate in a safe and sound manner, running day-to-day operations within an established risk profile, while protecting the interests of clients and other stakeholders (Mehran, 1995).

According to Maher, & Anderson (1999) “Good corporate governance includes, well-articulated corporate strategy against which the overall success and the contribution of individuals can be measured. The CG sets and enforces clear assignment of responsibilities, decision-making authority and accountabilities that is appropriate for the companies risk profiles. CG enables strong financial risk management function.

Andrei Shleifer (1997) indicates that the stock exchange through plays a major role in the economic development of our nation or any other country. It is through the stock market that companies seek capital from the stock exchange. In the recent past the performance of the stock market activities has reduced due to loss of confidence by the investors. Some brokers have been involved in market malpractices such as dealing in their clients shares without authority. The share brokers can manipulate the market by buying/selling huge quantities of a particular company’s share in order to alter the share prices radically for their personal gain. These shares are bought in the stockbroker’s name.

These are then sold to their clients at high profits, and commissions. This leads to unwarranted speculations, (Sabeshen 2008). The slump of activities in the Nairobi Stock Exchange due to loss of confidence calls for need to investigate the factors that affect the financial performance
of companies listed in the Nairobi Stock Exchange. The potential investors have lost trust in the stock market due to malpractice and professional negligence. To protect investors from losses, the capital regulations were amended to require the stockbrokers to secure professional indemnity insurance. (Capital Market Authority Annual Report & Accounts 2009).

1.2 Statement of the Problem

Listed firms can only achieve their objectives and effectively discharge their responsibilities if they are led by quality and effective leadership which is responsive, transparent and accountable, abide by the highest standards of fiduciary management. Listed firms’ failures have been attributed to bad corporate governance. The predominant and widely held view is that board size, board composition, and ownership concentration have a direct bearing on the performance of firms as they guarantee firm control on top management without compromising efficiency.


Madut, (2011) investigated the influence of corporate governance on the performance of stock brokerage firms in Kenya. His findings indicate that corporate governance can significantly enhance the performance of stock brokerage firms in Kenya while helping to avert the
problems of mismanagement witnessed in the recent past leading to collapse/liquidation of six brokerage firms in a short span of time. It is against this backdrop that this study seeks to examine how board size, independent directors and CEO duality affect the performance of firms listed in the Nairobi stock exchange.

1.3: Objective of the study

1.3.1: General objective

The general objective of the study was to investigate the effect of corporate governance on the financial performance of companies listed in the Nairobi stock Exchange.

1.3.2: Specific Objectives of the study

i. To find out the effects of board size on the financial performance of firms listed in NSE.

ii. To establish the effect of board composition on financial performance of firms listed in NSE.

iii. To ascertain the effects of ownership concentration on the financial performance of firms listed in NSE.

iv. To establish the effect of sustainable responsible business on the financial performance of companies listed in the NSE.

1.4: Research Questions

The study sought information to address the following questions:

i. What effects does board size pose on the financial performance of firms listed in NSE?

ii. Does the board composition affect the financial performance of firms listed in NSE?
iii. What effects does ownership concentration have on the performance of companies listed in the NSE?

iv. Does sustainable responsible business have an effect on the financial performance of companies listed in the NSE?

1.5: Significance of the study

This study will provide an insight to Kenyan companies as to the importance of proper Board size and composition, sustainable responsible business and the ownership concentration by examining its effects on the financial performance of the company. The findings from the study are useful in that they provide companies with commonly working board compositions and proper ownership structures. This information will be useful especially when companies are designing their competitive strategies with regard to Board composition and ownership structures.

This study will benefit the stockbrokers themselves, the institutional investors, retail investors, potential investors, listed companies that intends to raise capital through the stock exchange. The study will also benefit the Capital Markets Authority. This study will also be significant as it will add some more knowledge to the existing studies and thus will be used by other researchers as literature review.

1.6: Scope of the study

This study was limited to companies listed in the Nairobi stock exchange in the entire five categories i.e. agricultural sector, commercial and services, industrial and allied and finance, and investment sectors and alternative market segment. Data on the financial ratios and the independent variables were obtained from the financial statements of the companies in the CMAL (capital market authority library) from the year 2004 to present.
1.7: Limitation and delimitations of the study

Several setbacks limited the effectiveness of the study.

The time/duration for the research conducted was too short to cover all aspects of the study. The other limitation was the unavailability of some financial statements in the library as the copies might have been torn or lend to other researchers.

To counter these limitations the researcher had a budget which was followed to the letter. The researcher also had a project schedule and utilized the critical path in order to find the shortest time possible to complete the project. The researcher also gave an allowance to collect data from previous years to compensate for the missing data.
CHAPTER TWO
LITERATURE REVIEW

2.1 Introduction

This chapter covers the literature review on the effect of Corporative Governance on financial performance of companies listed at stock markets. It identifies previous studies in the area and provides the opportunity to evaluate other people’s works.

2.2 Theoretical review

2.2.1 The Shareholder Model

According to the shareholder model the objective of the firm is to maximize shareholder wealth through allocative, productive and dynamic efficiency; that is to maximize profits. The standard by which performance is judged here can generally be taken as the market value (shareholder value) of the firm. The principal problem of this model of corporate governance arises from the principal-agent relationship arising from the separation of beneficial ownership and executive decision-making. Thus although investors are interested in maximizing shareholder value, managers on the other hand may have objectives such as maximizing their salaries, growth of market share, or an attachment to particular investment projects (Jensen and Meckling - 1976).

Therefore the shareholders model is primarily concerned finding ways to align the interests of managers with those of the investors, hence ensuring the flow of external funds to firms and that financiers get a return of their investment. An effective corporate governance framework is one that minimizes the agency costs and bottleneck problems associated with the separation of ownership and control (Mehran, 1995).
According to Boatright, (2002), strengthening the shareholder’s right is important so that shareholders have a greater incentive and ability to monitor management, which can be achieved through enhancing the rights of legal protection of investors from exploitation by managers. Another means of enhancing governance in this model is to use indirect means of corporate control such as that provided by capital markets, managerial labor markets and markets for corporate control like takeovers.

2.2.2 The Stakeholder Model

The stakeholder model takes a wider view of the firm. Traditionally, according to this model, the corporation is responsible to a wider constituency of stakeholders other than shareholders. Other stakeholders may comprise of contractual partners such as employees, suppliers, customers, creditors and social constituents such as the society within which the firm is located, environmental interests, local and national governments (Chatterjee, 2009).

The problem here is to meet or fulfill the wider and diverse objectives of all these stakeholders. Nevertheless, due to the potential influence of corporate governance on performance, the notion that corporation have responsibilities to parties other than shareholders merits consideration. This considerations based on the impact of the specific stakeholder have on the behavior and performance of the firm and economic growth.(Andrei Shleifer 1997)

According to Williamson, (1985) in the stakeholder model, corporate governance is primarily concerned with how effective different governance systems are in proving long-standing investment and commitment amongst the various stakeholders. According, to the new stakeholder model the best firm is one which have committed suppliers, customers and employees. Corporate governance in this model is regarded as a set of institutional
arrangements for governing the relationship among all the stakeholders that contribute firm specific assets. (Williamson 1995).

Brickley & James (1987) indicate that the promotion of capital markets is also important for sector development. Industry sectors that rely on external funding are favored in outside systems, where there is strong protection of minority shareholders and more transparency. Active equity market is also important as it encourages innovative activity, entrepreneurship and the development of a dynamic small and medium sized enterprise (SME) sector.

According to Cho, (1998), active financial markets are linked with economic development, and then regulations that promote stock market activity may provide one of the underlying sources for economic growth. For instance, the protection of minority shareholders, which is linked to the development of stock markets, is critical to enhancing innovative entrepreneurship, and the development of sectors that rely on external funding.

Canyon, and Leech (1993) indicated that the monitoring of management depends basically on the discipline of capital markets, which is thought to serve as a particularly effective device for disciplining managerial behavior. For example, share prices are expected to fall whenever management fails to maximize shareholders value, exposing the firm to the threat of take-over bid and the removal of inefficient management. Nevertheless, liquid stock markets, strict trading rules, and equitable disclosure of information are necessary in order for the market for the corporate control to act as effective disciplining device.

According to Ezzamel, and Watson (1997), the board of directors is largely responsible for monitoring managerial performance and achieving an adequate return for shareholders, while preventing conflicts of interests and balancing competing demands on the corporation. Thus, whenever necessary the board also has the authority to replace the management for the
corporation. The board is also responsible for reviewing key executive and board remuneration.

Boatright, (2002) indicates that for the board to effectively fulfill their monitoring role they must have some degree of independence from management. Though, the emphasis in the outsider system is on independence, in reality there is the very serious problem that like management, the board too can become entrenched. This is particularly the case when the board members are compensated for their activities, and are themselves responsible for overseeing executive and board remuneration, which attracts high quality individuals. According to DeAngelo and Rice (2004), this in turn can interfere with performance, since service on too many board members reduces the monitoring ability of the board. This draws in the investors to control the move, which still brings in the problem of separation of ownership and control.

2.2.3 Agency Theory

Agency theory refers to relationship between two persons, one of whom must be a principal (owner) and the other, an agent (manager) agency theory therefore, is the theory that explains how best the agency relationship can be used for purpose of governing an organization (Brown governance Inc, 2004).

The principals and agents have specific core responsibilities which facilitate good governance of corporations. Principals are charged with three core responsibility in agency governance, i.e. to select and put in place the auditors (external independent body that audits and reports on integrity of manual reporting and controls), and ensure that there is an efficiency governance system in place. The agents are responsible for day today operations and other activities throughout the organization (Sarbanes-Oxley, 2004) the division of responsibility,
which is inherent in the agency governance mechanism, make it possible for accountability to be achieved since the flow of power and authority is well defined and understood in the organizations.

According to De Andres Azofra & Lupez (2005), the objective of the organization is to maximize shareholder wealth through efficiency. The firms’ performance is judged in this model by profitability and shareholder value. Therefore, managers and directors have an implicit responsibility to ensure that organizations are run in the best interest of the shareholders. The challenge in agency theory arises from the principal agent relationship occasioned by separation of ownership and executive decision making.

Jensen and Meckling (1976) further define agency relationship and identify agency cost. Agency relationship is a contract under which one or more persons (agent) to perform some services on the behalf, which involves delegating some decision making authority” conflict of interest between managers or controlling shareholders refer to the tendency that the former may extract “perquisites” (or perks) out of the firm’s resources and be less interested in pursuing new profitable ventures. Agency cost includes monitoring expenditure by principle such as auditing, budgeting control and compensation systems bonding expenditure by the agent and residual loss due divergence of interest between the principal and agent.

Fama (1980) argues that separation of ownership and control can be explained as result of efficient form of economic organization. The theory prescribe stronger directorship and shareholder control, it advocates fundamental function of Board of directors to control managerial behavior and ensure that managers acts in interest of shareholders
2.2.4 Management Theory

The proponents of management theory contend that the modern corporation is complete and, only sophisticated, experienced and professional management team can effectively direct and control it. Management theorists posit that agency theory was perhaps workable for the simpler, smaller corporations of Adam Smith’s days, but in today’s world, corporations are large, complex, multi-faceted entities that are challenging to direct and control (Brown Governance Inc: 2004).

Fabozzi & Modigliani (1995) argue that it is however, plausible to observe that under management theory, direction and control have been ceded by owners and boards (principals and governors) to the management team. The result is a breakdown in accountability as the correct separation of powers (division of duties) fails to occur. According to a Cadbury report produced in 2005, this arrangement vests immense discretionary powers on management who may misuse the powers to enhance their prestige and wealth at the expense of the principals.

Finkelstein, and Hambrick, (1996) indicates that there is no denying the fact that the modern organization is complex, but it is inappropriate in terms of accountability to allow managers inordinate discretionary latitude over both governance (direction and control) and day-to-day management. In fact, Adam Smith’s position is that the more complex social organizations get, the more people need to specialize, to divide their labor in order to enhance efficiency and internal control.

According to Cadbury report (2005), boards (governors) are not given responsibility for governance because they understand the corporation any better than managers, but precisely because they are not the managers. It is argued that one of the reasons Japan has failed to
completely recover from its economic troubles of the early 1990’s is because of its continued adherence to management theory (Brown Governance Inc; 2004).

2.2.5 Stakeholder Theory

Firth et al. (2006) state that a basis stakeholder theory is that companies are so large and their impact on society so pervasive that they should discharge accountability to many more sectors of society than solely their shareholders. Not only are stakeholders are affected by companies but they in turn affect companies in some way. They hold a “stake” rather than simply a ‘share’ in the companies’ stakeholders includes shareholders employees, suppliers, customers’ creditors’ and communities in the vicinity of the company’s operation and the public in general.

According to OECD (1999) good corporate governance helps to ensure that corporations take into account the interest of a wide range of constituencies, as well as of the communities within they operate and their boards are accountable to the company, and the shareholders. This, in turn, helps to assure that corporations operate for the benefit of society as a whole.

According to Ingley, & Van der Walt, (2005), the corporations should be socially responsible institutions managed in the public interest the modern corporations is more sensitive to matters of social responsibility and the environment, since this issues are the very heart of the society that gives the corporations charter to operate. It is well understood that corporations draws its inputs from society (labors, raw material managers finances), and sends back its products or services to the same society.

The negative side of the traditional stakeholders is that it’s difficult, if not possible, to ensure that corporation fulfills the larger objective of all their stakeholders and as such the decision
making process is very slow. Such decisions are often revisited even when strategic direction is approved. Blair (1995) argues that the idea failed to give clear guidance to help managers and directors set priorities and decide among competing socially beneficial lists of corporate resources and provide no obvious enforcement mechanisms, to ensure that corporations lined up to their social obligations.

2.2.6 Stewardship Theory

Stewardship theory argues that managers are inherently trustworthy and not prone to misappropriate corporate resources. Donaldson and Davies (1994) try to agree with the arguments of the stewardship theory that managers are good stewards of the corporation and diligently work to attain high levels of corporate profits and shareholder returns.

Jensen & Meckling (2006) argue that stewardship theory would suggest that control be centralized in the hands of the firm managers. The theory appears to motivate the top management and fails to take the knowledge of the rampant cases of failures of managerial integrity, and managerial competence. This omission makes the stewardship theory inadequate framework of analyzing corporate governance mechanism in the modern corporation.

Stewardship theorists assume that managers are good stewards to the firm. They are trustworthy and work diligently to attain high corporate profits and shareholders returns these stewards can cooperate and work closely with the principal to achieve a goal alignment (Davis et al 1997). Agency theory appears to effectively mitigate all the inadequacies of the other governance theories (managerial and stewardship theory). The principle of agency theory is applicable to both private and public sector and all other social organizations.
2.3 Empirical review

2.3.1 The Concept of Performance

Performance refers to output results and their outcome obtained from processes, products and services that permit evaluation and comparison relative to goals, standards, past results and other organizations. Performance can be expressed in non-financial and financial terms. Johnson, (1996) indicates that Performance Management includes activities to ensure that goals are consistently being met in an effective and efficient manner. Performance management can focus on the performance of an organization, a department, Employee, Processes to build a product or service.

Chatterjee (2009) indicates that the performance management process is a method of management design to ensure the organization and all its components are working together to optimize the organizations goals. Sidney and Horwitz. (2007) indicate that to achieve this design, performance management process must address the overall organization performance in conjunction with the components. The performance management process requires several ongoing activities. This include identifying and prioritizing goals, defining what constitutes progress towards goals, setting standards for measuring results, and tracking progress toward goals.

2.3.1.1 Financial performance

Finkelstein and Hambrick, (1996) indicates that one way of establishing references and managing the financial affairs of an organization is to use ratios. Ratios are simply relationships between two financial balances or financial calculations. These relationships establish references for understand how well a company is performing financially. Ratios also
extend the traditional way of measuring financial performance; i.e. relying on financial statements.

Firth et al (2006) indicates that for publicly traded companies, the relationship of earnings to equity or Return on Equity is of prime importance since management must provide a return for the money invested by shareholders. Return on Equity is a measure of how well management has used the capital invested by shareholders.

Johnson et al (1996) state that return on Equity indicates the percent returned for each dollar (or other monetary unit) invested by shareholders. Return on Equity is calculated by dividing Net Income by Average Shareholders' Equity. Return on Equity has three ratio components. The three ratios that make up Return on Equity are: Profit Margin = Net Income / Sales, Asset Turnover = Sales / Assets and Financial Leverage = Assets / Equity (Long and Malitz, 2005).

Mayer (1996) indicates that profit Margin measures the percent of profits you generate for each dollar of sales. Profit Margin reflects your ability to control costs and make a return on your sales. Profit Margin is calculated by dividing Net Income by Sales. Management is interested in having high profit margins. Asset Turnover measures the percent of sales you are able to generate from your assets. Asset Turnover reflects the level of capital we have tied-up in assets and how much sales we can squeeze out of our assets. Asset Turnover is calculated by dividing Sales by Average Assets. A high asset turnover rate implies that we can generate strong sales from a relatively low level of capital. Low turnover would imply a very capital-intensive organization, (Long and Malitz, 2005).

Financial Leverage is another component of Return on Equity. Financial Leverage is a measure of how much we use equity and debt to finance our assets. As debt increases, we financial leverage increases. Generally, management tends to prefer equity financing over
debt since it carries less risk. The Financial Leverage Ratio is calculated by dividing Assets by Shareholder Equity. Another financial performance indicator is the Liquidity Ratios which help understand the company can meet its obligations over the short-run. Higher liquidity levels indicate that the company can easily meet their current obligations (Mehran, 1995).

According to Long and Malitz, (2005), several types of ratios can be used to monitor liquidity. These include current ratio which is current assets divided by current liabilities. Current assets include cash, accounts receivable, marketable securities, inventories, and prepaid items. Current liabilities include accounts payable, notes payable, salaries payable, taxes payable, current maturity's of long-term obligations and other current accruals. A low current ratio would imply possible insolvency problems. A very high current ratio might imply that management is not investing idle assets productively. Generally, a company should have a current ratio that is proportional to its operating cycle.

Chatterjee (2009) notes that since certain current assets (such as inventories) may be difficult to convert into cash, a company may want to modify the Current Ratio. Also, if it uses the LIFO (Last In First Out) Method for inventory accounting, its current ratio will be understated. Therefore, the company will remove certain current assets from our previous calculation. This new ratio is called the Acid Test or Quick Ratio; i.e. assets that are quickly converted into cash will be compared to current liabilities. The Acid Test Ratio measures the company's ability to meet current obligations based on the most liquid assets. Liquid assets include cash, marketable securities, and accounts receivable. The Acid Test Ratio is calculated by dividing the sum of liquid assets by current liabilities.

Murphy, (2005) indicates that the other financial indicator is the Ratio of Operating Cash Flow to Current Debt Obligations which places emphasis on cash flows to meet fixed debt
obligations. Current maturities of long-term debts along with notes payable comprise our current debt obligations. We can refer to the Statement of Cash Flows for operating cash flows. Therefore, the Ratio of Operating Cash Flow to Current Debt Obligations is calculated; Operating Cash Flow / (Current Maturity of Long-Term Debt + Notes Payable).

Chatterjee (2009) indicates that another group of detail ratios is asset management ratios. Asset management ratios measure the ability of assets to generate revenues or earnings. They also compliment the liquidity ratios. They include Accounts Receivable Turnover (measures the number of times we were able to convert our receivables over into cash. Higher turnover ratios are desirable. Accounts Receivable Turnover is calculated as Net Sales / Average Accounts Receivable), Days in Receivables (The Number of Days in Accounts Receivable is the average length of time required to collect our receivables. A low number of days is desirable. Days in Accounts Receivable is calculated as:365 or 360 or 300 / Accounts Receivable Turnover).

McConnel, and Servaes (1990), indicate that inventory Turnover is measuring how many times the company turn their inventory over during the year. They state that higher turnover rates are desirable as this ensures that the performance of the company is good. A high turnover rate implies that management does not hold onto excess inventories and inventories are highly marketable.

McConnel, and Servaes (1990), elaborates that inventory Turnover is calculated as: Cost of Sales / Average Inventory), Days in Inventory (Days in Inventory is the average number of days a company holds inventory before a sale. A low number of inventory days is desirable. A high number of days imply that management is unable to sell existing inventory stocks. Days in Inventory is calculated as: 365 or 360 or 300 / Inventory Turnover). Capital Turnover
measures our ability to turn capital over into sales. Calculated as: Net Sales / Interest Bearing Debt + Shareholders Equity.

Mayer, (1996) states that other performance measures used to evaluate the efficiency of an investment or to compare the efficiency of a number of different investments are return on equity and return on investment. To calculate ROI, the benefit (return) of an investment is divided by the cost of the investment; the result is expressed as a percentage or a ratio. The amount of net income returned as a percentage of shareholders equity.

Mather & Andersson, (1999) deduced that return on equity measures a corporation's profitability by revealing how much profit a company generates with the money shareholders have invested. ROE is expressed as a percentage and calculated as: Return on Equity = Net Income/Shareholder's Equity.

2.3.2 Corporate governance

According to the United Nations Economic Commission of Africa (UNECA, 2002) good corporate governance exists in economic activity is un-impeded by corruption and other activities inconsistent with the public trust and where the institutions of government have the capacity to manage resource efficiently, can formulate, implement and enforce sound policies and regulations, can be monitored and be held accountable and have respect for the rules and norms of social and economic interactions.

As such, from a corporation perspective, the key elements contributing to an environment of good corporate governance and transparency enabling environment for private sectors development and growth, and institutional development and effectiveness (UNECA 2003). According to Rossouw (2003), there are many obstacles that frustrate the quest for good corporate governance such as: - general lack of effective regulatory and institutional
frameworks, lack of discipline and transparency, fear that the greater scrutiny of their corporate activity and disclose demands that go along with being listed can be exploited by the state and competitors.

Mueller, 2005), indicates that insufficient incentives for enterprises to list and thus enter the domain where the standards of the corporate governance is required and enforced, and a poor example of good corporate governance often set by state owned enterprises (Corporations) as this the board of directors do not display either competence or the independence that is required for good corporate governance.

According to UNECA (2002) in recognition that the responsibility for governance issues lies first and must be committed to improve governance for reasons as to execute public management functions in accountable manner, to demonstrate transparent and particularly economic policy making and execution as well as an open flow of information evaluate to all stakeholders. A number of codes of corporate governance initiatives have been adopted such as Kenya Private Sector Corporate Governance Trust, 1999 (PSCGT) based on the international standards (Ngugi, 2003)

Roc (2004), states that national codes emphasize the ethical nature of good Corporate Governance and special emphasizes is placed on the fact that good corporate governance is based on the following fundamental values: transparency, accountability, responsibility and probity. The various aspect of corporate governance that play a major role to realize these fundamental values are for example the importance of the role of boards of the institutions, risk management and reporting disclosure.

In addition Round, (2006), states that, Corporations refers to the mechanisms through which corporations and their management are governed. As such, it involves a set of relationship
among an organization management, its board of directors, its shareholders and its stakeholders. It furthermore provides structures through which objectives and monitoring of performance are determined to ensure sound corporate governance. The following is required; an established and seamless institutional and legal framework and pursuit of objectives that are supported by the board and management and that represent the interest of the organization and to shareholders.

2.3.2 The effect of corporate governance on performance

Reilly & Brown (1997) states that the term corporate governance has been used in various ways and boundaries of the subject differ widely. In the debate of economics the impact of corporate governance on performance, there are generally two different models of the corporation, the shareholder model and the stakeholder model. Prowse, (2004) states that in its narrowest logic; shareholder model, corporate governance often describes the formal system of accountability of senior management to shareholders. In its widest logic; stakeholder model, corporate governance can be used to describe the network of formal and informal relations involving the corporation.

A study done by Maher M. and Anderson T. of the Organization for Economic Co-operation and Development Secretariat (1999) shown that corporate governance has got an effect on both corporate performance and economic performance. The study gave a more explicit exposition of the shareholder and stakeholder models of corporate governance. There are underlying factors that promote efficient corporate governance and each corporate governance system has its own strengths, weaknesses and economic implications that are associated with each. The study provided empirical evidence on the link between corporate governance, firm performance and economic growth.
Reilly & Brown (1997) states that corporate governance framework can impinge upon the development of capital markets, innovative activity, entrepreneurship, the development of an active SME sector, and resource allocation, which consequently impinge upon the growth of the economy. It impacts upon the behavior and performance of firms. In the current time of growing capital mobility and globalization, corporate governance has become an important framework condition affecting the industrial competitiveness.

Simiyu (1992) indicates that transition economies, privatization has raised concerns on the way in which private enterprises should be governed. Poor corporate governance in many of such countries has proved, partially, to be a key impediment to improving competitiveness of firms. Thus better corporate governance should manifest itself in enhanced corporate performance and can lead to higher economic growth.

Corporate governance practices vary not only across countries but also firms and industry sectors, with the most striking difference being in the ownership and control of firms. Corporate governance systems can be distinguished according to the degree of ownership and control and the identity of controlling shareholders, (McConnel, and Servaes, 1990).

Traditionally, corporate governance has been associated with the “principal-agent” or “agency” problem. A “principal-agent” relationship arises when the person who owns a firm is not the same as the person who manages or controls it. For instance, investors or financiers (principals) hire managers (agents) to run the firm on their behalf. The investors need their managers to generate returns on their investments, and managers may need the investors’ since they may not have enough capital of their own to invest. In such a case there is a separation between the financing-ownership and the management of the firm –control (Berle and Means -1932).
2.3.4 Sustainable responsible business (SRB)

Reilly & Brown (1997) defines Sustainable responsible business (SRB), responsible business, or corporate social performance, as a form of corporate self-regulation integrated into a business model. Generally, CSR policy would function as a built-in, self-regulating system whereby business would monitor and ensure its support to law, ethical standards, and global norms. Subsequently, business would embrace responsibility for the impact of its activities on the environment, consumers, employees, communities, stakeholders and all other members of the public sphere. Development business ethics is one of the kinds of applied ethics that examines ethical principles and moral or ethical problems that can arise in a business environment.

In addition Round, (2006), adds that business ethics which is also known as corporate ethics is a form of applied ethics or professional ethics that examines ethical principles and moral or ethical problems that arise in a business environment. This applies to all aspects of business conduct and is relevant to the conduct of persons and business organizations as a whole. Business ethics can be both a normative and a descriptive discipline. As a corporate practice and a career specialization, the field is primarily normative.

Long and Malitz, (2005) indicates that finance is a social science discipline. The discipline shares its border with behavioral science, sociology, economics, accounting and management. Finance being a discipline dealing with technical issues such as the optimal mix of debt and equity financing, dividend policy, and the evaluation of alternative investment projects, and more recently the valuation of alternatives, futures, swaps, and other derivative securities, and portfolio diversification.
In the capital markets, fairness in trading practices, trading conditions, financial contracting, sales practices, consultancy services, tax payments, internal audit, and external audit should be ensured. Things like insider trading, securities fraud, bucket shops, forex scams are all common issues in manipulation of the financial markets (Boatright, 2002).

Executive compensation is necessary to ensure active and efficient equity market, concerns excessive payments made to corporate CEO's and top management should not be allowed. Bribery, kickbacks, and facilitation payments; while these may be in the (short-term) interests of the company and its shareholders, these practices may be anti-competitive or offend against the values of society (Round, 2006).

2.3.5 The Board Size

According to Capital Markets Authority Act (2005), ultimate responsibility is typically placed with the board of directors (Supervisory Board). The board is answerable to shareholders for the safeguarding of their interest through the lawful, informed, efficient, and able administration of the institution. The members of the board usually delegate the day-to-day management of daily business to officers and employees, but cannot abdicate responsibility for the consequences of unsound or imprudent policies and practices concerning malpractices in the stock market.

The Board of directors of an organization is a key mechanism to monitor manager’s behavior and to advise them. The largely shared wisdom regarding the optimal board size is that the higher the number of directors sitting on the board the less is performance. This leans on the idea that communication, coordination of tasks, and decision making effectiveness among a large group of people is harder and costlier than it is in smaller groups, (Belkhir, 2006).
Limiting board size to a particular level is widely believed to improve the performance of the firm at all levels. Benefits arising from increased monitoring by larger boards are outweighed by poorer communication and cumbersome decision-making. Empirical studies on board size seem to provide the same conclusion: A big board is likely to be less effective in substantive discussions of major issues among themselves in monitoring management. Large boards are less effective and are easier for CEO to control (Lipton and Lorsch, 1992). In this case, Board size plays a major role on the performance of every prospering organization.

The required number of board of members varies among jurisdictions, but in all cases should include more than one executive member. In brokerage systems that use the supervisory board model, all members are usually nonexecutives. Despite the strength of this approach, the lack of involvement in policy setting by wholly nonexecutive boards is a major deficit. Boards with only one executive member, board members will have a broader perspective and will be able to look at the company though the eyes of more than one senior executive, (Belkhir, 2006).

2.3.6 Board composition

Globalization and liberalization of financial markets, corporate governance scandals and increasing demands of stakeholders for accountability and transparency of organizations, brought the roles and tasks of board of directors (BODs) to the center of corporate governance debate (Ingley and Van der Walt, 2005). BODs have various and important roles (Finkelstein and Money, 2003).

According to Zahra and Pearce (1989), the main roles of BODs are control, service and strategy. Realization of these roles mainly depends on the characteristics of boards, which affect the performance of organizations. Research reviews and meta-analyses consistently
indicate equivocal relationships between board composition, leadership structure and organizational performance (Johnson et al, 1996).

Belkhir, (2006) states that the leadership provided by the boards of directors of many troubled institutions has often been found to be ineffective. One of the chief functions of independent (nonexecutive) directors should therefore be the avoidance of economic and legal mistakes that may threaten the life of their broker. When a properly functioning board of directors exists, problems discovered by internal control or external auditors should be immediately brought to its attention.

Lipton and Lorsch, (1992) insinuates that a board must be strong, independent, and actively involved in its broker’s affairs. Both the brokerage firm’s directors and the executive management must adhere to high ethical standards and be fit and proper to serve. Although the company’s directors will not necessarily be experts on brokerage, they should have the skills, knowledge, and experience to enable them to perform their duties effectively. The most important duty of the board is to ensure that the management team has the necessary skills, knowledge, experience, and responsible manner. The management team should be directly accountable to the board, and this relationship should be supported by robust structures.

According to Firth et al (2006), during good times, a board sets tone and direction. It oversees and supports management efforts, testing and probing recommendations before approving them, and make sure that adequate controls and systems are in place to identify and address concerns before they become major problems. During bad times, an active, involved board can help a broker survive if it is able to evaluate problems, take corrective actions, and when necessary keep the broker’s problems resolved.
2.3.7 Ownership concentration

Ownership structure is the identity of company ownership and an important element of corporate governance which is potentially important. Ownership structure consists of two type, dispersed ownership to outside investors and concentrated ownership, (Surya et al, 2005). Ownership concentration is determined by the number of share that is held by three biggest shareholders and counted with Herfindahl index (HSF) which is the square amount of share proportion (in percent), (Firth et al, 2006). Investor protection is high when the management ownership is high because outside investors expect the manager with their share ownership significantly will act in the best interest of all the shareholders to minimize the negative impact from unanticipated crisis of their share, (Leung et al, 2007).

Durnec and Kim (2003) claim that the bigger the ownership that owned by the controller shareholders and it will improve the quality and performance of a firm. Gomes (2010), proves that a high ownership concentration can give a trustable commitment from the controller owner with a purpose to build reputation and not to misuse the interest of minority shareholders. In this regard, ownership concentration factor is one of the determinants in the performance of listed firms in NSE.

According to Firth et al, (2006), an effective board should have a sound understanding of the nature of the broker’s business activities and associated risks. It should take reasonable steps to ensure that management has established strong systems to monitor and control those risks. Even if members of the board are not experts in brokerage risks and risk management systems they should ensure that such expertise is available and that the risk management system undergoes appropriate reviews by suitably qualified professionals. In their study Maria Maher and Thomas Anderson (1999), of the organization for economic and cooperation and
performance of the effect of corporate governance on firm performance they found out that firms that have strong internal controls with board members segregating duties of management levels perform better.

A study conducted by Leung et al, (2007), found out that internal controls in a business environment are often enforced through segregation of duties in business processes. Different roles and responsibilities are assigned to each individual to provide a check and balance environment appropriate to the risk level of the business. Segregation of duties is a naturally embedded into the hierarchical and compartmentalized structure of any business organization.

2.4 Conceptual Framework

Diagram showing effects of corporate governance on financial performance of companies listed in the Nairobi stock exchange.

Figure 2.1 conceptual framework

Source: Developed for the study 2012
CHAPTER THREE
RESEARCH METHODOLOGY

3.1 Introduction

This chapter contains the research design, the target population and sample frame, data collection instrument and procedures and data analysis methods.

3.2 Research Design

The research was longitudinal. According to Orodho (2002), this is a type of research method in which subjects is tested one or more times after initial testing. Typically, subjects are assigned randomly to an experimental group (e.g. a group that performs a specific type of training) and a control group after the initial testing. Both the experimental and the control groups are tested again simultaneously one or more times during the period of the study.

In this case, companies listed in NSE will be involved to provide necessary information which is useful in building conclusions on the factors that will be discussed. Longitudinal studies allow researchers to gather information, summarize, present and interpret for the purpose of clarification the design was chosen because the researcher gathered data on the state of affairs in the study location without manipulating any variables.

3.3 Target Population

Target population is defined as all the members of a real or hypothetical set of people, events or objects to which a researcher wishes to generalize the results of the research study (Borg and Gall, 1989). The target population for this study comprised companies listed under agricultural, commercial and services, industrial and allied and alternative investment segments on the NSE.
3.4 Sampling strategy

3.4.1 Sampling Frame

For this study, the sampling frame was companies listed in the NSE. The sampling frame was divided into strata i.e. Agricultural, commercial and services, industrial and allied and alternative investment. According to the NSE 2012, there are 58 companies listed in the stock exchange which are divided in these four categories. Since not all the 58 companies were listed as the sampling frame, a stratified frame was used to obtain the companies.

3.4.2 Sampling and Sampling Procedures

Sampling means selecting a given number of subjects from a defined population as representative of that population. Any statements made about the sample should also be true of the population (Orodho, 2002). It is however agreed that the larger the sample the smaller the sampling error.

The study used stratified random sampling to select 30 companies listed in the stock exchange. These made up the strata. This method involved dividing the population into five significant strata based on the sector they fall under. Simple random sampling technique was used to pick the target companies from each stratum.

A sample size of more than 30 or at least 10 percent is usually recommended for social sciences (Cooper and Schindler, 2003; Kotler, 2001). The study utilized 30 companies listed percent of the population; the sample size is considered appropriate (Mugenda & Mugenda, 2003).
3.5 Data Collection procedure
The main tools of data collection for this study were secondary data from Journals in the capital market authority, internet and websites of the sampled companies. In order to increase reliability of the findings, a combination of data from annual financial reports was used.

3.5.2 Data Collection Procedure
The secondary data was particularly very important in the study. The researcher collected important information from the library books, annual reports, journals and publications from research institutions.

3.6 Reliability
Cronbach's alpha was used to test the reliability of the instrument and data collected from the financial statements. According to Cooper, & Schindler, (2000) Cronbach's alpha is a measure of internal consistency, that is, how closely related a set of items are as a group. A "high" value of alpha is often used (along with substantive arguments and possibly other statistical measures) as evidence that the items measure an underlying (or latent) construct. Cronbach's alpha is a coefficient of reliability (or consistency).

3.7 Validity
Validity is defined as the accuracy and meaningfulness of inferences, which are based on the research results (Mugenda and Mugenda, 1999). In other words, validity is the degree to which results obtained from the analysis of the data actually represents the phenomena under study. Validity, according to Borg and Gall (1989) is the degree to which a test measures what it purports to measure. All assessments of validity are subjective opinions based on the judgment of the researcher (Wiersma, 1995).
Validity is concerned with the extent to which the measurement and therefore the data obtained are relatively free from error (are accurate). Wainer and Braun (1998) describe the validity in quantitative research as “construct validity”.

### 3.8 Data Analysis Plan

This research yielded data that was utilized in the analysis. Quantitative analysis entailed analyzing numbers about a situation by choosing specific aspects of that situation. Descriptive statistics was used to analyze the quantitative data obtained.

Quantitative data analysis requires the use of a computer spreadsheet, and for this reason the Statistical Package for Social Sciences (SPSS) was used. As Martin and Acuna (2002) observe, SPSS is able to handle large amount of data, and given its wide spectrum of statistical procedures purposefully designed for social sciences, it is also quite efficient.

Multiple regression models was used to determine the relative importance of each independent variable on financial performance of the companies listed. The model is as follows:

\[ P = \alpha + \beta_1 BS + \beta_2 BC + \beta_3 OC + \beta 4 SRB + \varepsilon \]

Where;

\( P \) = Performance

\( \alpha \) = a constant

\( \beta_1 \) = coefficient of Board size

\( BS \) = Board size

\( \beta_2 \) = coefficient of Board composition
B = Board composition

β_3 = Coefficient of Ownership concentration

OC = Ownership concentration

β_4 = Coefficient of Sustainable responsible business

SBR = Sustainable responsible business

ε = Error term
CHAPTER FOUR
DATA ANALYSIS AND PRESENTATION OF RESULTS

4.0 Introduction
This chapter presents the findings of the study, Effects of Corporate Governance on the Financial Performance of Companies Listed in the Nairobi Securities Exchange. Analysis is done using statistical package for social sciences (SPSS) linear regression analysis. Analysis of each variable is independents in order to bring out the effect of the dependent variables on the independent variable.

4.1 Response rate
The study targeted 30 companies listed at the Nairobi securities exchange. 28 out of the target companies had complete financial statements dating from 2004 - 2011. This represents a response rate of all the 95%. This response rate is considered as good and was achieved through the anxious efforts made by the researcher to ensure a reliable response.

Table 4.1 Response rate

<table>
<thead>
<tr>
<th>Departments</th>
<th>Sample</th>
<th>Data obtained</th>
</tr>
</thead>
<tbody>
<tr>
<td>Agriculture</td>
<td>3</td>
<td>3</td>
</tr>
<tr>
<td>Commercial and Services</td>
<td>6</td>
<td>5</td>
</tr>
<tr>
<td>Finance and Investment</td>
<td>8</td>
<td>8</td>
</tr>
<tr>
<td>Industrial and Allied</td>
<td>9</td>
<td>8</td>
</tr>
<tr>
<td>Alternative Market Segment</td>
<td>4</td>
<td>4</td>
</tr>
<tr>
<td>Total</td>
<td>30</td>
<td>28</td>
</tr>
</tbody>
</table>

Source: survey data, (2012)
4.1.1 Validity

To test the validity of the data collected from the financial statements, the data collected and entered into SPSS and a validity test conducted. From the validity test conducted it was evident that all the data obtained were valid, this is proved by the cronbach alpha results where all the sectors under consideration recorded very high alpha results.

Table 4.2 Reliability results

<table>
<thead>
<tr>
<th>Values</th>
<th>Variables</th>
<th>Number of Items</th>
<th>Cronbach Alpha</th>
</tr>
</thead>
<tbody>
<tr>
<td>Agriculture</td>
<td></td>
<td>3</td>
<td>0.856</td>
</tr>
<tr>
<td>Commercial and Services</td>
<td></td>
<td>5</td>
<td>0.877</td>
</tr>
<tr>
<td>Finance and Investment</td>
<td></td>
<td>8</td>
<td>0.793</td>
</tr>
<tr>
<td>Industrial and Allied</td>
<td></td>
<td>8</td>
<td>0.912</td>
</tr>
<tr>
<td>Alternative Market Segment</td>
<td></td>
<td>4</td>
<td>0.781</td>
</tr>
</tbody>
</table>

Source: survey data, (2012)

4.2 Board size

The study was to examine the board audit committee size and its composition whether it has any effect on the performance of companies listed in the NSE. The results in table 4.3 indicated that the average size of directors who served on the board were eight (8) members. The average standard deviation of was 2.68 coupled with a maximum board size of 18 board members and a minimum board size of four 4 board members suggested that these boards were widely dispersed but the average size of 8 persons is essentially good for firm performance.
According to researchers such as Jensen (1993) and Lipton & Lorsch (1992) argued that extreme large board sizes are less effective for firm performance as it is difficult for them to make a decision that is agreeable to everyone at the shortest time. Also with large boards it is difficult to coordinate where all members are required to attend meetings. Raheja (2005) added that larger boards have higher coordination costs especially if there are many international directors which the company is required to facilitate for their travel and other expenses.

Most of companies listed in the NSE have a board size of more than 5 board members. The finance and investment sector had the highest number of board members scoring a mean score of 12.1 meaning that most of the companies had at least 12 board members. Some banks like standard chartered bank have a board size of 17 members whereas some like diamond trust bank of Kenya has 5 board members. Companies listed under the agricultural sector had the least number of board members averaging 5.7. Companies such as Rea Vipingo have a board size of five members.

Table 4.3: Mean and standard deviations of board size

<table>
<thead>
<tr>
<th>Item</th>
<th>Mean*</th>
<th>S.d</th>
</tr>
</thead>
<tbody>
<tr>
<td>Agriculture</td>
<td>5.7931</td>
<td>.75846</td>
</tr>
<tr>
<td>Commercial and Services</td>
<td>10.5690</td>
<td>.94982</td>
</tr>
<tr>
<td>Finance and Investment</td>
<td>12.0966</td>
<td>.84955</td>
</tr>
<tr>
<td>Industrial and Allied</td>
<td>8.0690</td>
<td>.05426</td>
</tr>
<tr>
<td>Alternative Market Segment</td>
<td>7.0846</td>
<td>.92804</td>
</tr>
</tbody>
</table>

Source: survey data, (2012)
4.3 **Board composition**

The board composition in this study was determined on two different perspectives; one was the composition of the women serving in the board, which was taken as a ratio of total women in the board by the total board members. The other one was the composition of non executive directors serving in the board which was measured as the ratio of total non executive directors by the total board members.

From the descriptive results in table 4.2 it was clear that the average mean score of women serving in the board was low probably because the selected companies listed in the NSE Nairobi were offering their services to mix clientele (both male and female) that gave opportunity men to dominate in the boards. Considering the number of board members in the table 4.3 above, it was clear that the proportion of women serving in the boards was subsequently small in the agricultural sector considering the number of board members.

Hartarska (2004) pointed out that boards with higher proportions of women on the board reach more and poorer borrowers, and have higher return on assets. On the other hand boards of selected companies were deemed more independent shown by the relatively higher mean score of non executive directors with an average mean of 3.81 memberships. Coleman and Biekpe, (2005) pointed out that many non executive directors make independent decision without the influence of internal governance that is the management. It is being assumed that many non executive directors are composed of members with diverse skills and experience that enhance performance of companies (Jensen, 1993).
The selected companies that had audit committees on their boards were having members size of the audit committee ranging from 2-5 members, with an average size of about 4 members. Kyereboah – Coleman and Biekpe (2005) pointed out that, in an ideal case, a strict independent audit committee is made up solely of non-executive directors and non-affiliates of the institution (directors who have worked in the institution before) and the minimum size of audit committee should be 3 members and at least one member should be from the institutions probably the internal auditor who reports direct to the board.

From the analysis showed on table 4.5 the audit committees of the commercial and service sector had the highest dominance of non-executive directors with a mean of 11.08 of members in the boards therefore one could say that these institutions to a large extent had independent audit committees. The audit committee independence is measured by total non-executive directors in audit committee by the total audit committee members.

The findings of this study are in line with a study conducted by Belkhir, (2006) who states that the leadership provided by the boards of directors of many troubled institutions has often been found to be ineffective. One of the chief functions of independent (non-executive) directors should therefore be the avoidance of economic and legal mistakes that may threaten the life of their company. When a properly functioning board of directors exists, problems discovered by internal control or external auditors should be immediately brought to its attention.
Table 4.4: Mean and standard deviations of board composition

<table>
<thead>
<tr>
<th>Item</th>
<th>Mean*</th>
<th>S.d</th>
</tr>
</thead>
<tbody>
<tr>
<td>Agriculture</td>
<td>3.0846</td>
<td>.92804</td>
</tr>
<tr>
<td>Commercial and Services</td>
<td>8.0690</td>
<td>.05426</td>
</tr>
<tr>
<td>Finance and Investment</td>
<td>11.0846</td>
<td>.23414</td>
</tr>
<tr>
<td>Industrial and Allied</td>
<td>5.3224</td>
<td>.20951</td>
</tr>
<tr>
<td>Alternative Market Segment</td>
<td>4.1784</td>
<td>.22346</td>
</tr>
</tbody>
</table>

4.4 Ownership concentration

All the companies listed in the NSE were determined whether they had dispersed ownership to outside investors or concentrated ownership. Concentrated ownership was assigned a value of 1 whereas dispersed ownership was assigned a value of 2. From the data collected from financial statements it was clear that majority of the companies listed at the NSE had dispersed ownership with existence of many shareholders possessing little shares each.

From the data collected it can observed that the performance of companies listed in the NSE should be good sentiments brought forward by a study conducted by Durnec and Kim (2003) who claim that the bigger the ownership that owned by the controller shareholders and it will improve the quality and performance of a firm.

This is because a study conducted by Gomes (2010), proves that a high ownership concentration can give a trustable commitment from the controller owner with a purpose to build reputation and not to misuse the interest of minority shareholders. In this regard, ownership concentration factor is one of the determinants in the performance of listed firms in NSE.
Table 4.5 Descriptive statistics of ownership concentration

<table>
<thead>
<tr>
<th></th>
<th>Mean</th>
<th>Deviation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Agriculture</td>
<td>1.9667</td>
<td>.96431</td>
</tr>
<tr>
<td>Commercial and Services</td>
<td>1.2000</td>
<td>.84690</td>
</tr>
<tr>
<td>Finance and Investment</td>
<td>1.9000</td>
<td>.95953</td>
</tr>
<tr>
<td>Industrial and Allied</td>
<td>1.2000</td>
<td>.80516</td>
</tr>
<tr>
<td>Alternative Market Segment</td>
<td>1.3333</td>
<td>.71116</td>
</tr>
</tbody>
</table>

4.5 Sustainable responsible Business

In this study sustainable responsible business was determined by the extent to which companies listed ensured fairness in trading practices, trading conditions, financial contracting, sales practices, consultancy services, tax payments, internal audit, and external audit.

A five point likert's scale was used to analyze the extent to which companies listed in the NSE were practicing SRB and it was evident that companies in the financial and investment sectors were involved more in SRB than companies in other sectors. This is evident from the mean score obtained from 4.1 in a five point scale. The high scores were achieved by the unavailability of excessive payments received by the board members of the financial and investment sectors.

This study is supported by Round, (2006) who indicates that executive compensation is necessary to ensure active and efficient equity market, concerns excessive payments made to corporate CEO's and top management should not be allowed. Bribery, kickbacks, and facilitation payments; while these may be in the (short-term) interests of the company and its shareholders, these practices may be anti-competitive or offend against the values of society.
### Table 4.6: Mean and standard deviations of sustainable responsible business

<table>
<thead>
<tr>
<th>Item</th>
<th>Mean*</th>
<th>S.d</th>
</tr>
</thead>
<tbody>
<tr>
<td>Agriculture</td>
<td>2.7931</td>
<td>.75846</td>
</tr>
<tr>
<td>Commercial and Services</td>
<td>3.5690</td>
<td>.94982</td>
</tr>
<tr>
<td>Finance and Investment</td>
<td>4.0966</td>
<td>.84955</td>
</tr>
<tr>
<td>Industrial and Allied</td>
<td>3.0690</td>
<td>.05426</td>
</tr>
<tr>
<td>Alternative Market Segment</td>
<td>3.0846</td>
<td>.92804</td>
</tr>
</tbody>
</table>

#### 4.6 Financial Performance

To establish the financial performance of companies listed in the Nairobi stock exchange, ratios, return on assets, return on equity and return on investment were used.

Return on assets is an indicator of how profitable a company is relative to its total assets. It was determined by dividing a company's annual earnings by its total assets. From the analysis, it can be established that management in the financial and investment sector was the most significant sector as far the return on assets is concerned with a mean score of 0.682. The lowest sector as far as return on assets is concerned was the agriculture sector with a mean score of 0.0065.

Return on investment is a performance measure used to evaluate the efficiency of an investment or to compare the efficiency of a number of different investments. In this study, it was calculated as benefit (return) of an investment divided by the cost of the investment; the result was then expressed as a ratio and the mean score determined. Findings from the study revealed that the agricultural sector was the highest as far as the return on investment is concerned with a mean score of 0.85. Commercial and service sector was the lowest though with a mean score of 0.34.
Return on equity was determined as the amount of net income returned as a percentage of shareholders equity. Return on equity was used to measure profitability by revealing how much profit a company generates with the money shareholders have invested. From the study it was evident that companies listed under the financial and investment sector experienced the highest returns on equity with a mean score of 0.5341 followed by companies listed under the agriculture sector 0.4375.

Table 4.7: Mean and standard deviations of sustainable responsible business

<table>
<thead>
<tr>
<th>Sector</th>
<th>Return on assets</th>
<th>Return on invest</th>
<th>Return on equity</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Mean*</td>
<td>S.d</td>
<td>Mean*</td>
</tr>
<tr>
<td>Agriculture</td>
<td>0.0065</td>
<td>0.0619</td>
<td>0.8500</td>
</tr>
<tr>
<td>Commercial and Services</td>
<td>0.1605</td>
<td>0.8669</td>
<td>0.3405</td>
</tr>
<tr>
<td>Finance and Investment</td>
<td>0.6820</td>
<td>0.7987</td>
<td>0.8257</td>
</tr>
<tr>
<td>Industrial and Allied</td>
<td>0.0156</td>
<td>0.0341</td>
<td>0.8000</td>
</tr>
<tr>
<td>Alternative Market Segment</td>
<td>0.2103</td>
<td>0.8431</td>
<td>0.6607</td>
</tr>
</tbody>
</table>

4.7 Regression analysis

A multivariate regression analysis was used to investigate the extent to which explanatory variables captured in the model contribute to the explained variance in the dependent variable. The model takes the ROA, ROI and ROE as proxies of financial performance. The
explanatory variables include Board Size, board composition; sustainable responsible business and ownership concentration were used to determine the financial performance.

4.7.1 Return on assets (ROA)

Table 4.8 Results of regression results using ROA as the Predicted Variable

<table>
<thead>
<tr>
<th>Model summary</th>
<th>Model</th>
<th>R</th>
<th>R Square</th>
<th>Adjusted R Square</th>
<th>Std. Error of the Estimate</th>
<th>Significance.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>1</td>
<td>0.295a</td>
<td>0.087</td>
<td>0.072</td>
<td>2.25222</td>
<td>0.001b</td>
</tr>
</tbody>
</table>

ANOVAa

<table>
<thead>
<tr>
<th>Model</th>
<th>Sum of Squares</th>
<th>df</th>
<th>Mean Square</th>
<th>F</th>
<th>Sig</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 Regression</td>
<td>87.767</td>
<td>3</td>
<td>29.256</td>
<td>5.767</td>
<td>0.001b</td>
</tr>
<tr>
<td>Residual</td>
<td>918.123</td>
<td>181</td>
<td>5.073</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>1005.889</td>
<td>184</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Coefficients

<table>
<thead>
<tr>
<th>Model</th>
<th>Un-standardized Coefficients</th>
<th>Standard coefficients</th>
<th>t</th>
<th>Sign</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>B</td>
<td>Std Error</td>
<td>Beta</td>
<td></td>
</tr>
<tr>
<td>1 (constant)</td>
<td>1.891</td>
<td>1.001</td>
<td></td>
<td>1.890</td>
</tr>
<tr>
<td>Board Size</td>
<td>0.235</td>
<td>0.072</td>
<td>0.231</td>
<td>3.248</td>
</tr>
<tr>
<td>Board composition</td>
<td>0.019</td>
<td>0.011</td>
<td>0.203</td>
<td>1.770</td>
</tr>
<tr>
<td>Ownership concentration</td>
<td>0.198</td>
<td>0.904</td>
<td>0.025</td>
<td>0.220</td>
</tr>
<tr>
<td>Sustainable responsible</td>
<td>0.021</td>
<td>0.086</td>
<td>0.045</td>
<td>0.654</td>
</tr>
</tbody>
</table>

a. Predictors (constant), board size, board composition, ownership concentration and sustainable responsible business.

b. Dependent Variable: Return on Assets
Results obtained from the data analysis revealed that there is a positive relationship between ROA and board size, board composition, ownership concentration and sustainable responsible business. The coefficients p – values are given in the parenthesis. The estimated model coefficients, (p- values) indicate the statistical significance of a result that is the degree to which the result is true. for Board Size, the estimated model coefficients, the p – values were less that 0.05 (i.e. p = 0.001 < 0.05) respectively implying that board composition, ownership concentration and sustainable responsible business are all statistically significant in predicting ROA at 5 % significance level.

\[ \text{ROA} = 1.890 + 0.231X_1 + 0.203X_2 + 0.025X_3 + 0.045X_4 + 1.001 \]

The model indicates that for every one unit increases in Board Size, ROA increases by a factor of 0.231 while for every one unit increase in Board composition ROA increases by a factor of 0.203 and for an increase of Ownership concentration ROA increases by a factor of 0.025. an increase of Sustainable responsible business by 1 unit, ROA increases by 0.045 units.

The purpose of analysis of Variance (ANOVA) is to test for significant differences between means. To test for significant differences between means, ANOVA was conducted. F – test is used when comparing statistical models that have been fitted to a data set, in order to identify the model that best fits the population from which the data was sampled. F – test therefore plays an important role in the Analysis of Variance.

Table 4.8 shows the results of F test which tests whether the ratio of the four independent variables estimates is significantly greater than 1. The results show an F value of 5.767
indicating that the test is highly significant. That implies that the means for the explanatory variables are significantly different from each other.

The fitted model was diagnosed and found to be statistically significant at 5% significant level (regression p-value = 0.001 < 0.05). This shows that the combination of board size, board composition, ownership concentration and sustainable responsible business (Performance as measured by ROA) The adjusted R-Square value is an indicator of how well the model fits the data, hence showing the strength of a model in forecasting. Furthermore, adjusted R-square = 0.072, implying that the independent variables accounted for 7.2% of the dependent variable.
### 4.7.2 Return on Equity

Table 4.9 Results of regression results using ROE as the Predicted Variable

<table>
<thead>
<tr>
<th>Model summary</th>
<th>Model</th>
<th>R</th>
<th>R Square</th>
<th>Adjusted R Square</th>
<th>Std. Error of the Estimate</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>1</td>
<td>0.321&lt;sup&gt;a&lt;/sup&gt;</td>
<td>0.103</td>
<td>0.087</td>
<td>13.50203</td>
<td>0.000&lt;sup&gt;b&lt;/sup&gt;</td>
</tr>
</tbody>
</table>

**ANOVA**<sup>a</sup>

<table>
<thead>
<tr>
<th>Model</th>
<th>Sum of Squares</th>
<th>df</th>
<th>Mean Square</th>
<th>F</th>
<th>Sig</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 Regression</td>
<td>3790.413</td>
<td>3</td>
<td>1263.472</td>
<td>6.931</td>
<td>0.001&lt;sup&gt;b&lt;/sup&gt;</td>
</tr>
<tr>
<td>Residual</td>
<td>3297.186</td>
<td>181</td>
<td>182.305</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>36787.602</td>
<td>184</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**Coefficients**

<table>
<thead>
<tr>
<th>Model</th>
<th>Un-standardized Coefficients</th>
<th>Standard Coefficients</th>
<th>t</th>
<th>Sign</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>B</td>
<td>Std Error</td>
<td>Beta</td>
<td></td>
</tr>
<tr>
<td>1 (constant)</td>
<td>0.089</td>
<td>0.060</td>
<td></td>
<td>3.849</td>
</tr>
<tr>
<td>Board Size</td>
<td>0.262</td>
<td>0.434</td>
<td>0.205</td>
<td>0.906</td>
</tr>
<tr>
<td>Board composition</td>
<td>0.218</td>
<td>0.065</td>
<td>0.383</td>
<td>0.371</td>
</tr>
<tr>
<td>Ownership concentration</td>
<td>0.211</td>
<td>0.417</td>
<td>0.215</td>
<td>0.885</td>
</tr>
<tr>
<td>Sustainable responsible</td>
<td>0.231</td>
<td>0.561</td>
<td>0.026</td>
<td>0.914</td>
</tr>
</tbody>
</table>

**Notes:**

- Predictors – (Constant), board size, board composition, ownership concentration and sustainable responsible business.
- Dependent Variable: Return on Equity

The coefficients p-values of the fitted regression model (given in the parenthesis) were less than 0.05 for the constant (i.e. \(p = 0.000 < 0.05\)). The relationship between ROE and board size, board composition, ownership concentration and sustainable responsible business is statistically significant at 5% significance level. The relationship can be summarized as follows:

\[
ROE = 0.089 + 0.262X1 + 0.218X2 + 0.211X3 + 0.231X4 + 0.060
\]
Notably, the degree to which board size, board composition, ownership concentration and sustainable responsible business predict ROE is less than that which they predict ROA by 0.026, 0.18, 0.034 and 0.19 respectively. Again the fitted model indicate that for every one unit increase in Board size, ROE increases by a factor of 0.262 while for every one unit increases in board composition ROE increases by a factor of 0.218. Furthermore, ROE increases by a factor of 0.211 whenever the ownership concentration is increased by 1 unit and 0.231 whenever sustainable responsible business is increased by 1 unit.

To test significant differences between means, ANOVA was conducted. As shown in Table 4.9 the results of F test, $F=6.931$ is significantly greater than 1 implying that the means for the explanatory variables are significantly different from each other. The regression model $P$-value $= 0.000 < 0.05$ implies that the model is statistically significant at 5% significance level. However, adjusted $R$-square $=0.087$, implying that the independent variables accounted for 8.7% of the dependent variable.
4.7.3 Return on investment (ROI)

Table 4.10 Results of regression results using ROI as the Predicted Variable

<table>
<thead>
<tr>
<th>Model summary</th>
<th>Model</th>
<th>R</th>
<th>R Square</th>
<th>Adjusted R Square</th>
<th>R</th>
<th>Std. Error of the Estimate</th>
<th>Significance</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>1</td>
<td>0.325&lt;sup&gt;a&lt;/sup&gt;</td>
<td>0.106</td>
<td>0.091</td>
<td>7.57739</td>
<td>0.001&lt;sup&gt;b&lt;/sup&gt;</td>
<td></td>
</tr>
</tbody>
</table>

ANOVA<sup>a</sup>

<table>
<thead>
<tr>
<th>Model</th>
<th>Sum of Squares</th>
<th>df</th>
<th>Mean Square</th>
<th>F</th>
<th>Sig</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 Regression</td>
<td>1227.887</td>
<td>3</td>
<td>409.296</td>
<td>7.128</td>
<td>0.000&lt;sup&gt;b&lt;/sup&gt;</td>
</tr>
<tr>
<td>Residual</td>
<td>10392.442</td>
<td>181</td>
<td>57.417</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Total</td>
<td>11620.329</td>
<td>184</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
</tbody>
</table>

Coefficients

<table>
<thead>
<tr>
<th>Model</th>
<th>Un-standardized Coefficients</th>
<th>Standard coefficients</th>
<th>t</th>
<th>Sign</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>B</td>
<td>Std Error</td>
<td>Beta</td>
<td></td>
</tr>
<tr>
<td>1 (constant)</td>
<td>11.958</td>
<td>3.367</td>
<td>-</td>
<td>3.552</td>
</tr>
<tr>
<td>Board Size</td>
<td>0.769</td>
<td>0.244</td>
<td>0.222</td>
<td>3.154</td>
</tr>
<tr>
<td>Board composition</td>
<td>-0.114</td>
<td>0.036</td>
<td>-0.358</td>
<td>-3.152</td>
</tr>
<tr>
<td>Ownership concentration</td>
<td>-0.882</td>
<td>0.040</td>
<td>-0.183</td>
<td>-1.606</td>
</tr>
<tr>
<td>Sustainable responsible business</td>
<td>0.021</td>
<td>0.222</td>
<td>0.391</td>
<td>1.082</td>
</tr>
</tbody>
</table>

a. Predictors (constant), board size, board composition, ownership concentration and sustainable responsible business.

b. Dependent Variable: Return on Assets

Results obtained from the data analysis revealed that there is a positive relationship between ROI and board size and sustainable responsible business. The results also reviewed that there would be an increase in ROI if the board size and sustainable responsible business were increased.
was a negative correlation between ROI and board composition and ownership concentration. The coefficients p – values are given in the parenthesis. The estimated model coefficients, (p-values) indicate the statistical significance of a result that is the degree to which the result is true. for Board Size, the estimated model coefficients, the p – values were less that 0.05 (i.e. p = 0.001 < 0.05) respectively implying that board composition, ownership concentration and sustainable responsible business are all statistically significant in predicting ROI at 5 % significance level.

$$ROI = 3.552 + 0.769X1 - 0.114X2 - 0.882X3 + 0.021X4 + 3.367$$

The model indicates that for every one unit increases in Board Size, ROI increases by a factor of 0.769 while for every one unit increase in Board composition decreases by a factor of 0.114 and for an increase of Ownership concentration ROI decreases by a factor of 0.882. An increase of Sustainable responsible business by 1 unit, ROI increases by 0.021 units.

The purpose of analysis of Variance (ANOVA) is to test for significant differences between means. To test for significant differences between means, ANOVA was conducted. F – test is used when comparing statistical models that have been fitted to a data set, in order to identify the model that best fits the population from which the data was sampled. F – test therefore plays an important role in the Analysis of Variance.

Table 4.8 shows the results of F test which tests whether the ratio of the four independent variables estimates is significantly greater than 1. The results show an F value of 7.128 indicating that the test is highly significant. That implies that the means for the explanatory variables are significantly different from each other.
The fitted model was diagnosed and found to be statistically significant at 5% significant level (regression p-value = 0.001 < 0.05). This shows that the combination of board size, board composition, ownership concentration and sustainable responsible business. (Performance as measured by ROI) The adjusted R – Square value is an indicator of how well the model fits the data, hence showing the strength of a model in forecasting. Furthermore, adjusted R – square = 0.106 implying that the independent variables accounted for 10.6% of the dependent variable.
CHAPTER FIVE
SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.0 Introduction

This chapter presents a summary of the findings, as regard to the objectives of the study, also the conclusion is drawn based on the findings. Recommendations and area for further research is highlighted in within the chapter.

The overall objective of the study was to investigate the Effects Of Corporate Governance On The Financial Performance Of Companies Listed In The Nairobi Securities Exchange data was collected from the capital market authority library Annual financial reports for companies listed in the security exchange. This chapter summarizes the findings, draws conclusions and makes recommendations to policy makers, regulatory authorities, professionals, and industry stakeholders.

5.1 Summary of Findings

The findings of this study were summarized around the specific objectives of the study which were to examine the board size, board composition, ownership concentration and sustainable responsible business and and effects on the performance of companies listed at the NSE.

The objectives were achieved through data collected using a structured questionnaire that captures all the corporate governance and performance variables and additional information collected through secondary data. Performance of the companies listed at the NSE was measured using return on Assets (ROA), Return on equity (ROE) and Return on investment and corporate governance structures were measured by board size, board composition (non executive directors), ownership concentration and sustainable responsible business.
All the objectives are the research questions. The objectives of this study were aimed at establishing relationships between board size, board composition, ownership concentration and sustainable responsible business extent to which these governance variables influence performance.

The analysis involved the use of the value of R and R-squared to determine the strength of the relationship between independent variables and indicators of financial performance. It was intended to investigate the extent to which the identified explanatory variables influence the dependent variable.

The findings of this study indicate that Board Size, board composition (non executive directors), ownership concentration and sustainable responsible business influence the performance of companies listed at the NSE. Furthermore, the findings indicated that there is a positive relationship between all the variables in corporate governance and performance.

The findings showed that on average, performance of all the companies as measured by ROA and ROE is 0.217 and 0.15 respectively whereas the average board size in the industry is 7.21. A Board size of 7.21 is closest approximation of board members in all the sectors as addressed by the study.

With regard to performance measures, the results for Board size was found to be statistically significant at 5% significance level with \( p < 0.05 \). Board Size had p-values of 0.001, 0.002 and 0.004 for ROA, ROI and ROE while for Independent Directors, the p-values were 0.078, 0.001 and 0.001 for ROA and ROE. Independent Directors was therefore found not to be
5.2 Answers to research questions

5.2.1 What effects does board size pose on the financial performance of firms listed in NSE?
From the study it can be observed that the board size has a significant effect on the financial performance of companies listed at the NSE. This is statistically proven by the fact that results obtained from the data analysis revealed that there is a positive relationship between ROA, ROI and ROE and board size. Hence there is a positive relationship between financial performance and board size.

5.2.2 Does the board composition affect the financial performance of firms listed in NSE?
To answer this research question, statistics prove that there is a positive relationship between ROA, ROE and board composition. However there was a negative relationship between the same variable and ROI.

5.2.3 What effects does ownership concentration have on the performance of companies listed in the NSE?
Form the data collected from financial statements it was clear that majority of the companies listed at the NSE had dispersed ownership with existence of many shareholders possessing little shares each. Thus to answer this research question, statistics prove that there is a positive relationship between ROA, ROE and board composition. However there was a negative relationship between the same variable and ROI.

5.2.4 Does sustainable responsible business have an effect on the financial performance of companies listed in the NSE?
In all the financial performance variables considered i.e. ROA, ROE and ROI, it can be observed that sustainable responsible business has a positive effect on the financial performance of companies listed at the NSE.
5.3 Conclusions

The study found that board diversity of a moderate board size with a considerable number of women should be encouraged in order to maintain relatively independent board and audit committee meetings are very important for the companies listed at the NSE performance.

It was also concluded that companies listed at the NSE’s boards have enhanced their effectiveness by tapping broader talent pools for their directors and that more diverse board is likely to have better relations with other stakeholders.

The findings of the study do not only aim at fine-tuning governance in companies listed at the NSE in terms of policy direction, but equally important to ensure that collapse of companies as a result of governance is forestalled.

5.4 Recommendations

It is evident that corporate governance structure has an influence on financial performance in companies listed in the NSE Kenya. Hence, there is a need to strike a good balance between quality and quantity with regards to board sizes. It is recommended that board size should be fairly large and not too large that will discourage investors especially shareholders. Also, the board size should be of quality with board members having diverse skills and experience. Again from the findings it shows that for the audit committee to be effective it is recommended to have a size of 3 to 5 members.

It is also recommended in tandem with others, that companies should make more use of non executive directors, also policies to promote gender diversity in governance have deemed appropriate therefore companies are required to increase the ratio of women on the board so as to ensure board independence, promote shareholder value by enhancing institution performance as this send a positive signal to potential investors and shareholders. It is
recommended that the board/audit committee should meeting frequently as this is likely to enhance performance of the companies.

5.5 Suggestions for Future Research

The current literature addresses a range of issues relating to corporate governance structures and firm performance. However, the debate on corporate governance continues, at an accelerated rate, both in academic circles and popular press, and both at domestic and international levels this shows that this field need more attention and study.

Although this study contributes to the body of literature on various dimensions, the results are not conclusive. Observations covering a period of seven years and in one country may not be representative, and the results may not be generally applicable to developing countries. The sample and choice of statistical analysis may also have shortcomings. The sample and choice of statistical analysis may also have shortcomings.

It would therefore, be desirable to extend the present study by complementing it with studies using other methods and including comparative data. The inclusion of other corporate governance and performance variables (such social performance indicators) as would also merit further consideration.

More research on individual board structures are needed to assess the effects on its performance. Also future study should look other factors such as share holders interest, board and CEO compensation to establish its effects on financial performance.
REFERENCE


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Leung, Sidney and Bertrand Horwitz. 2007. *Is Concentrated Management Ownership Value Increasing or Decreasing? Evidence in Hong Kong during the Asian Financial Crisis*. Journal of Economics Literature classification: G34; G10; G32; 120.


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State Street Corporation 2008, Investor Confidence Index Summary, 4th Quarter: Boston, USA.


World Bank study (2003), Framework for assessing corporate governance and financial risks


## Appendix 1: Companies Listed At the Nairobi Securities Exchange

### Agriculture
- Rea Vipingo Ltd
- Sasini Tea and Coffee Ltd
- Kakuzi Ltd

### Commercial and Services
- Access Kenya
- Marshall's EA
- Car and General
- Hutchings Biemer (suspended)
- Kenya Airways
- CMC Holdings
- Uchumi Supermarkets (suspended)
- Nation Media Group
- TPS (Serena)
- Scan Group
- Standard Group
- Safaricom

### Finance and Investment
- Barclays Bank of Kenya
- CFC Stanbic Bank
- Housing Finance
- Centum Investment
- Kenya Commercial Bank
• National Bank of Kenya
• Pan Africa Insurance Holding
• Diamond Trust Bank of Kenya
• Jubilee Insurance
• Standard Bank
• NIC Bank
• Equity Bank
• Olympia Capital
• Co-operative Bank of Kenya
• Kenya Re-Insurance

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<tr>
<th>Industrial and Allied</th>
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<tr>
<td>• Athi River Mining Ltd</td>
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<tr>
<td>• Carbacid Investments</td>
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<td>• EA Cables</td>
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<td>• EA Breweries</td>
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<td>Alternative Market Segment</td>
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## Appendix 2 Sample of Financial Statements

<table>
<thead>
<tr>
<th>S/No.</th>
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<th>Net Dividends</th>
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