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EFFECT OF CORPORATE GOVERNANCE ON FIRM PERFORMANCE

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Abstract

Purpose: This study sought to investigate the effects of corporate governance on firm performance among companies listed in NSE from 2006 to 2015.

Methodology: The study adopted a causal study design of the 55 listed firms in Nairobi Stock Exchange; however, the research used a sample of 35 firms. Secondary data was collected from audited annual financial statements. SPSS was used as the main data analysis tool. Both Descriptive and inferential statistics methods were applied to analyze the data.

Results: The study found that board independence had a positive and significant relationship with firm performance measured as return on assets and return on equity. The study also found out that board size had a negative and significant relationship with firm performance. Further the study found out there was a positive and significant relationship between CEO duality and firm performance .The study also found positive and significant relationship between board tenure and firm performance .The study found a positive and significant relationship between multiple directorship and firm performance.

Policy recommendation: The study concluded that companies should adopt policies that enhance board independence, CEO Duality and multiple directorships as they improve firm performance however there is need for listed companies to match their board size and board tenure with companies' specific needs.

Keywords: *Corporate governance,Capital market, Measures of firms Performance, CEO Duality*

1.0 INTRODUCTION

Corporate governance is critical to all economic transactions particularly in emerging and transition economies (Klein, 1998; Bhagat and Black, 2000). Likewise, corporate governance has assumed the centre stage for enhanced corporate performance (Hutchinson, 2002; Young, 2003; Weisbach, 2008). It has also been defined by Park and Shin (2003) to include the structures, processes, cultures and systems that engender the successful operation of organizations (Ayogo, 2005).

Many scholars, such as Musila (2007) argued that the erosion of investor confidence in Kenya was brought about by the country's poor corporate governance standards and a lack of transparency in the financial system. This is evidenced by the collapse of firms listed in the Nairobi Stock Exchange such as Uchumi and many stock brokerage firms in a period of just less than ten years. Therefore, the restoration of confidence in the economy by investors will rely on improvements in corporate governance standards, including the adoption of transparency as an important strategy in corporate management. With the economic recovery of most East African countries, attention has understandably been drawn to addressing and researching the underlying issues and factors that can lead to a crisis like that witnessed in the US (Jensen, 2001).

CEO duality is the practice of one person serving both as a firm's CEO and Board chair contribute to or inhibit firm performance depending on the perspective. This is probably one of the most important, controversial and inconclusive questions in corporate governance research and practice according to Finkelstein and D'Aveni, (1994). Two views, drawn from agency theory and stewardship theory, are directly at odds with each other. While agency theory suggests that splitting the board chair and CEO positions facilitates more effective monitoring and control of the CEO, and that a firm failing to do so may underperform those which split the two top positions stewardship theory, argues that CEO duality establishes strong, unambiguous leadership embodied in a unity of command and that firms with CEO duality may make better and faster decisions and, consequently, may out-perform those which split the two positions.

In recent years, Kenya has witnessed the collapse of many business enterprises and incurred tremendous costs due to weak corporate governance structures within the organizations. Despite the good laws that exist in theory, there is still a window for senior managers to misappropriate shareholder's wealth. Ms Priscilla Sampa, Lusaka Stock Exchange (LuSE) legal counsel and company secretary, while addressing a corporate governance workshop in Lusaka identified excessive compensation, improper loans, self-dealing, under performance or shirking as crucial pointers of sinister motives that the public should note (Wahome, 2009). This came in the height of Nairobi Stock Exchange report of low investor confidence levels due to weak corporate governance structures that cost investors billions in losses as traders irregularly traded in clients' shares.

One of such recent irregularities in Kenya involved Nyagah Stockbrokers. The firm was put under statutory management in 2008 after failing to meet its financial obligations. Consequently, over 25,000 investors lost vast amounts of money, lodging claims to the Capital Markets

Authority for compensation through the Investor Compensation Funds (ICF). The CMA spent Shs. 302 million to paying investors a maximum of Shs. 50,000, since the State cannot afford to compensate the full amount invested, Nyagah stockbrokers top management (owners and directors) assets must be sold in order to compensate each and every investor of the firm. Based on a forensic audit done by PricewaterhouseCoopers (PwC) that was leaked to the public, PwC reported the firm might have gone down with about Shs. 1.3billion of public funds and in addition to this diversion of funds by management, fraud by the staff, occurrences of collusion by other stockbrokers in the NSE, and even office of the regulator (Bonyop, 2009).

1.2 Problem statement

Kenya has been experiencing turbulent times with regard to its organizational practices and this has resulted in declining profits in the manufacturing sector of the economy (Mutindi, Namusonge&Obwogi, 2013). Statistics from World Bank show that large scale manufacturers operating in Kenya registered stagnation and declining profits for the last five years due to a turbulent operating environment (WB, 2014). It is estimated that large manufacturing firms have lost 70 per cent of their market share in East Africa largely attributed to contingencies (RoK, 2014a).Further statistics from Kenya Association of Manufacturers have shown that some firms announced plans to shut down their plants and shift operations to Egypt due to negative influences of contingencies (KAM, 2014). In 2014, manufacturing sector in Kenya contributed barely 10% to the GDP which represented 3.4 per cent growth to Sh.537.3 Billion indicating a decline from the previous year 2013 where it had reported a 5.6 per cent growth mainly due to a challenging operating environment and high operational costs (KNBS, 2014).

Many large Manufacturing firms have relocated or restructured their operations opting to serve the local market through importing from low-cost manufacturing areas such as Egypt therefore resulting in job losses (Nyabiage&Kapchanga, 2014) citing turbulent operating environment and high operating costs. This is an indication that many manufacturing firms in Kenya are experiencing performance challenges with many reporting profit warnings due to challenges in the operating environment (RoK,2014).

It is therefore inadequate to analyse firm's performance by financial performance especially under today's changing operating environment (Qi, 2010). The manufacturing sector in Kenya has a huge untapped potential contribution to employment and GDP if the challenges facing this sector are properly addressed (Wagana&Kabare, 2015).The study would eventually help in determining what is needed to stop manufacturing firms from failing, stagnating in performance or relocating from Kenya resulting to job losses and therefore continue in operation to the foreseeable future. The study therefore, seeks to understand the influence of leadership characteristics on performance of large manufacturing firms in Kenya.

Recent global events concerning high-profile corporate failures such as Enron in the US have put back on the policy agenda and intensified debate on the efficacy of corporate governance mechanisms as a means of increasing firm financial performance.

Failure to manage their businesses in a professional manner and serious governance malpractices has seen some stock brokers so far experience significant financial difficulties forcing the Capital Markets Authority to place them under receivership/statutory management (CMA Report, 2009). The firms listed in the NSE are supposed to serve as investing vehicles for the public and they are supposed to be managed professionally in order to attract investor confidence and safeguard the publics' interest. The placement of Uchumi under receivership in 2006 and eventual delisting from the NSE is just but an example. The responsibility for collapse of Uchumi then was placed right under the board of directors who were accused of ignoring governance structures and engaging in malpractices. This study aims at investigating the effect of corporate governance on firms performance of companies listed in NSE.

1.4 Specific Objectives

The study was based on the following specific objectives:

1. To ascertain the effect of board independence on firm's performance
2. To find out the effect of board size on firm's performance
3. To examine the effect of board tenure on firm's performance
4. To ascertain the effect of CEO duality on firm's performance
5. To find out the effect of multiple directorship on firm's performance of listed companies.

1.5 Research Hypothesis

The following null hypothesis was tested in the study:

$H0_1$: There is no significant effect of board independence on firms' performance.

$H0_2$: There is no significant effect of Board size on firm performance.

$H0_3$: There is no significant effect of board tenure on firm performance.

$H0_4$: There is no significant effect of CEO dualityon firm performance.

$H0_5$: There is no significant effect of multiple directorships on firm performance.

2.0 LITERATURE REVIEW

2.1 Theoretical review

2.1.1 Agency Theory

Jensen &Meckling (1976) in their extensive research to explain the managerial behavior of a given organization through integration of theory of property rights, agency theory so as to understand the ownership structure which greatly influence the behavior of an organization. In a situation where owners hire the series of managers to manage the affairs of a firm, principle agent relationship develops. Managers have increased the opportunity to engage in opportunistic behavior at the expense of the owner hence creating costs to the owner. The cost arises due to

imperfect information and risk aversion. The agency theory predicts that information asymmetry and moral hazards will be negatively related to the size of a firm, where, the bigger the size of a firm the smaller will be information asymmetry and moral hazards (Chittenden et al, 2002).

According to Jensen and Meckling (1976), there are a few kinds of conflicts of interests, namely, conflict of interest between shareholders and mangers on one hand and conflict of interest between shareholders and debt holders on the other hand. With respect to the conflict of interest between shareholders and managers, it is conditional on the promises that managers hold less than 100% residual claim of the firms. Consequently, they do not capture the fall bought from that enhancing effort. With regards to conflict of interest between debt holders and equity holders, managers often act as shareholder's interest at the instance of right incentives.

The theoretical framework upon which this study was based on was the agency theory which posits that in the presence of information asymmetry the agent (in this case, the directors and managers) is likely to pursue interests that may hurt the principal, or shareholder (Fama, 2000). At first the theory was applied to the relationship between managers and equity holders with no explicit recognition of other parties interested in the well-being of the firm. Subsequent research efforts widened the scope to include not just the equity holders but all other stakeholders, including employees, creditors, government, etc. This approach, which attempts to align the interests of managers and all stakeholders, has come to be regarded as the stakeholder theory.

The stakeholder theory has been a subject of some investigation. Jensen (2001) provides a comprehensive review of corporate governance, with a particular focus on the stakeholder theory. The authors note the presence of many parties interested in the well-being of the firm and that these parties often have competing interestsalthough equity holders might welcome investments in high yielding but risky projects, for example, such investments might jeopardize the interests of debt holders especially when the firm is teetering on the edge of bankruptcy. The review also emphasizes the role of non-market mechanisms, citing as an example the need to determine an optimal size of the board of directors especially in view of the tendency for board size to exhibit a negative correlation with firm performance. Other non-market mechanisms reviewed by Young (2003) include the need to design a committee structure in a way that allows the setting up of specialized committees with different membership on separate critical areas of operations of the firm. Such a structure would allow, for example, productivity-oriented committees and monitoring-oriented ones.

2.3 Empirical Review

2.5The Link between Board of Directors and Firm Performance

The board of directors is charged with oversight of management on behalf of shareholders. Agency theorists argue that in order to protect the interests of shareholders, the board of directors must assume an effective oversight function. It is assumed that board performance of its monitoring duties is influenced by the effectiveness of the board, which in turn is influenced by factors such as board composition and quality, size of board, duality of chief executive officer, board diversity, information asymmetries and board culture (Brennan, 2006).

The issue of structure of the board of directors as a corporate governance mechanism has received considerable attention in recent years from academics, market participants, and regulators. It continues to receive attention because theory provides conflicting views as to the impact of board structure on the control and performance of firms, while at the same time the empirical evidence is inconclusive. To date, the relationship between board structure (as opposed to board processes) and company performance has been the most studied aspect among all board investigations (Bhagat and Black, 1999). In these studies, it is often assumed that a company's financial performance is mainly determined by board characteristics.

2.5.1 The effects of Board Independence on Firm Performance

Board independence is the ability of the board to make their decisions without the interference from insiders in the organization. This is particularly useful when board members are drawn outside the organization and display high professionalism in their decision making process.

John and Senbet (1998) argue that a board is more independent if it has more non-executive directors. As to how this relates to firm performance, empirical results have been inconclusive. In one breath, it is asserted that executive (inside) directors are more familiar with a firm's activities and, therefore, are in a better position to monitor top management. On the other hand, it is contended that non-executive directors may act as "professional referees" to ensure that competition among insiders stimulates actions consistent with shareholder value maximization (Fama, 2000). Cotter *et al.*,(1997) support this view underscoring the important role of outside directors in protecting shareholders' interest through effective decision control.

Some authors have also found that there is no significant relationship between proportion of non-executive directors and firm performance (Bhagat and Black, 2002). It has been shown that the effectiveness of a board depends on the optimal mix of inside and outside directors (Baums, 1994). However, available theory is scanty on the determinants of optimal board composition (Weisbach, 2002). As for the relation between board independence and firm performance, if outside directors are independent and have professional ability, they could be more objective to make decisions and monitor managers.

2.5.2 The Effect of Board Size on Firm Performance

This is considered a crucial characteristic of the board structure. Large boards could provide the diversity that would help companies to secure critical resources and reduce environmental uncertainties (Goodstein *et al.*, 1995). According to Yermack (1996), coordination, communication and decision-making problems increasingly impede company performance, particularly, when the number of directors increases. A research done by Adams and Mehran (2003) indicate that bank holding companies have board size significantly larger than those of manufacturing firms.

A review of the empirical evidence on the impact of board size on performance shows mixed results. However, the results of Haniffa*et al*. (2006) are inconclusive. Using a market return

measure of performance, their results suggest that a large board is seen as less effective in monitoring performance, but when accounting returns are used, large boards seem to provide the firms with the diversity in contacts, experience and expertise needed to enhance performance. Yermack (1996) finds an inverse relationship between board size and firm value; in addition, financial ratios related to profitability and operating efficiency also appear to decline as board size grows. Finally, Connelly and Limpaphayom (2004) find that board size does not have any relation with firm performance.

2.5.3 The effect of Board Tenure on Firm Performance

In a competitive labor market, longer tenure reflects favorable perceptions of the board's ability (Milbourn, 2003), which suggests that board members are more likely to 'go along' with management on important managerial decisions to retain high quality boards. Incumbent directors are more likely to favor CEOs with long tenure because those that are strongly opposed are less likely to be re-nominated (Shivdasani and Yermack, 1999). Thus, long-serving CEOs are expected to have greater managerial power because of more influence over board members and superior ability/performance.

Studies on this board tenure shows that, there is relationship between board tenure and firm value, which is reflected in M&A performance, financial reporting quality, corporate strategies and innovation, executive compensation, and CEO replacement. The results indicate that, for firms with short-tenured boards, the marginal effect of board learning dominates entrenchment effects, whereas for firms that have long-tenured boards, the opposite is true. For long-tenured boards, transaction costs could take the form of agency costs. For instance, board tenure choice may reflect the extent to which CEOs have influence over the board selection process. Further, firms with staggered boards can only replace a portion of board member each year, in which case the use of a staggered board itself introduces agency problems (Bebchuk and Cohen, 2005). For short-tenured boards, transaction costs could take the form of frictions in the labour market for directors.

Empirical analysis on studies on this area shows that board tenure matters as it is related to firm value and corporate policies above and beyond other commonly examined firm and board characteristics. The results highlight a time-varying trade-off between knowledge and entrenchment for board effectiveness, which should be taken into account when designing board structure(Bebchuk and Cohen, 2005).

2.5.4 The Effect of CEO Dualityon Firms Performance

The question of whether the chairman and CEO positions should be separated has been controversial. The advantages and the drawbacks of separating the chairman and CEO positions have been studied extensively for instance: Combining the positions of chairman and CEO confers greater power to the CEO, Brickley,*et al*. (1997) finds that in most companies, CEOs gain the title of chairman after having outperformed their peers. They argue that the chairman title serves as a reward to a new CEO who has demonstrated superior performance and

represents an implicit vote of confidence by outside directors. In their view, requiring companies to separate the positions of CEO and chairman would deprive boards of an important tool to motivate and reward new CEOs.

However, bestowing the CEO and chairman duties in one individual makes it harder for a board to replace a poorly performing CEO, which can reduce the flexibility of a board to address large declines in performance (Goyal et *al*., 2002). Among large industrial companies, those with non-CEO chairmen traded at higher price-to-book multiples (Yermack, 1996).

Under CEO-chairman duality, the CEO of a company plays the dual role of chairman of the board of directors. There are two schools of thought on CEO-Chairman duality. Several researchers argue that CEO-chairman duality is detrimental to companies as the same person will be marking his "own examination papers". Separation of duties will lead to: (i) avoidance of CEO entrenchment; (ii) increase of board monitoring effectiveness; (iii) availability of board chairman to advise the CEO, and (iv)establishment of independence between board of directors and corporate management (Baysinger and Hoskisson, 1997).

On the other hand, other researchers believe that since the CEO and chairman are the same person, the company will: (i) achieve strong, unambiguous leadership; (ii) achieve internal efficiencies through unityof command; (iii) eliminate potential for conflict between CEO and board chair, and (iv) avoid confusion of having two public spokespersons addressing firm stakeholders (Davis, Schoorman and Donaldson, 1997). Consistent with these arguments, Cannella and Lubatkin (1998) report a positive link between a dual leadership structure and financial performance, Brickley, Coles, and Jarrell (1997) find a negative market reaction upon the announcement of splitting roles, whileDedman and Lin (2002) find no evidence of significant abnormal returns upon the announcement of splitting roles in the post-Cadbury period, and Simpson and Gleason (1999) report that companies that combine the roles the CEO and chairman are less likely to be financially distressed. A closer look at the empirical evidence reveals that the relationship between CEO-chairman duality and company performance is mixed and inconclusive.

2.5.5 The Effect of Multiple Directorships on Firms Performance

Multiple directorships are thought to signal director quality. Fama and Jensen (1983) argue that the market for multiple appointments creates incentives for directors to develop their reputation as good monitors. Studies by Gilson (1990), Coles and Hoi (2003), and Harford (2003) provide support for the notion that directors undertake decisions that are consistent with both the directors' creating reputational capital and provide them with additional appointments, increase their visibility, and provide lucrative commercial opportunities. Additionally, Booth and Deli (1995) suggest that multiple directorships permit firms to maintain advantageous relationships with their suppliers and customers, and further, the larger the firm, the more important these directorships become both to the firms and to the individuals.

However, other studies also suggest that too many directorships *lower* directorial effectiveness. Core *et al* (1999) reports that busy directors provide excessive compensation for their CEOs, which results in lower firm performance. Shivdasani and Yermack (1999) provide evidence that suggests that busy directors cater to the CEO, thus compromising their monitoring role. If this indeed is the case, busy directors may not fully represent shareholder interests. In a recent study Fich and Shivdasani (2006) show that firms with busy directors exhibit lower book-to-market ratios as well as weaker operating profitability. They also present results that suggest that if directors are busy, the rate of CEO turnover (in response to performance) is significantly lower than otherwise. Finally, if busy directors take on another appointment, the firms where they already serve exhibit negative abnormal returns.

In the U.S., professional bodies have also recognized the possible detrimental effects of multiple directorships. Ferris *et al*. (2003) cite reports by Council of International Investors (1998) and National Association of Corporate Directors (1996) that suggest that directors should not serve on more than two or three boards. The Business Roundtable (1997) by contrast believes that it is not necessary to impose limits on number of directorships. Finally, in a survey of directors of Fortune 500 companies, although the directors indicated that they turned down appointments due to lack of time, they did not support placing mandatory limits on the number of boards they could serve on.

2.7 Conceptual Framework

Independent variables **Dependent variable**

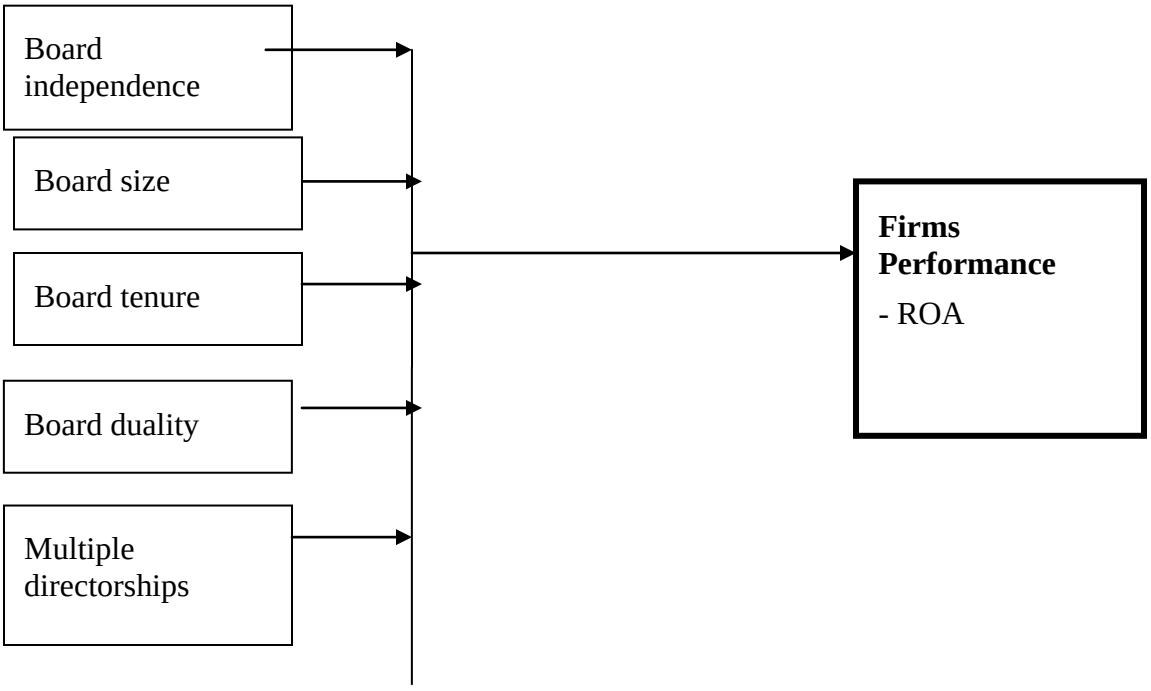

Figure 2.1 Conceptual Framework

Source: Author (2015)

3.0 METHODOLOGY

The study adopted a causal study design of the 55 listed firms in Nairobi Stock Exchange; however, the research used a sample of 35 firms. Secondary data was collected from audited annual financial statements. SPSS was used as the main data analysis tool. Both Descriptive and inferential statistics methods were applied to analyze the data

4.0 RESULTS FINDINGS

4.1 Descriptive Statistics

Table 1: A summary of firm corporate governance

Descriptive Statistics	Mean	Std. Deviation
Board Independence	0.47	0.22
Board Size	8.71	3.20
Board Tenure	5.69	1.92
CEO Duality	0.09	0.28
Multiple directorship	7.14	4.01
ROA	0.09	0.15

The results on table 1 above showed that the companies under study have an average board independence of 0.474314with a standard deviation of 0.22. This implied that the board of most of the companies were influenced by external and internal factors to a rating of 52.6% and thus had effect on their decision making process.

Board size had a mean of 8.71 and standard deviation of 3.2. Most of the boards had an average of 9 members. The mean value for CEO duality and multiple directorships are 0.09 and 5.69 respectively which indicates that most of the institutions had dual board membership and multiple directorships. The average ROA for the companies were 0.09 This implies that most of the companies were performing well in terms of the financials.

4.2Inferential Data Analysis

4.2.1 Correlation

In this section, the study measured the degree of association between the governance variables and firm's performance; the governance proxies such as board size, board independence, CEO Duality, Board Tenure and multiple directorship vis-à-vis the firm's performance. From the priority stated in the previous chapter, a positive relationship was expected between the measures of corporate governance and firms' performance.

Table 2: Correlation Analysis

Correlations		Board Independence	Board Size	Board Tenure	CEO Duality	Multiple directorship	ROA
Board Independence	Pearson Correlation	1.000					
	Sig. (2-tailed)						
Board Size	Pearson Correlation	.338**	1.000				
	Sig. (2-tailed)	0.000					
Board Tenure	Pearson Correlation	.241**	.212**	1.000			
	Sig. (2-tailed)	0.000	0.000				
CEO Duality	Pearson Correlation	0.048	.123*	0.055	1.000		
	Sig. (2-tailed)	0.371	0.021	0.308			
Multiple directorship	Pearson Correlation	.403**	.336**	.391**	0.04	1.000	
	Sig. (2-tailed)	0.000	0.000	0.000	0.453		
ROA	Pearson Correlation	.439**	.211**	.366**	.133*	.432**	1.000
	Sig. (2-tailed)	0.000	0.000	0.000	0.013	0.000	

** Correlation is significant at the 0.01 level (2-tailed).

* Correlation is significant at the 0.05 level (2-tailed).

The results on table 2 show that corporate governance variables have a positive and significant association with the firm performances of the listed companies. The result revealed a positive and significant association between board independence, board size, CEO Duality, board tenure, multiple directorships and firm performance (ROA) at a significance level of 0.000.

Results show that board independence is positively correlated with firm performance (ROA) as supported by significant p value of 0.000 and beta coefficient of 0.439. Similarly, the results show that board size is positively correlated and statistically significant with firm performance (ROA) as supported by significant p value of 0.000 and beta coefficient of 0.211. The results further indicated that board tenure is positively correlated and statistically significant with firm performance (ROA) as supported by significant p value of 0.000 and beta coefficient of 0.366.

The results further showed that CEO Dualityis positively correlated with ROA as supported by significant p value of 0.013 and beta coefficient of 0.133. However, CEO Dualityis positively correlated with ROE but statistically insignificant as supported by significant p value of 0.177 and beta coefficient of 0.072. Finally, the results revealed that multiple directorshipis positively correlated with firm performance (ROA,) as supported by significant p value of 0.000 and beta coefficient of 0.432. This reveals that any positive change in the corporate governance structureleads to increased firm performances.

4.2.2 Test for Multicollinearity

Multicollinearity occurs where two or more independent variables strongly influence each other. The presence of multicollinearity makes the estimation and hypothesis testing about individual coefficients in regression to have false significance values because multicollinearity makes the regression coefficient undefined or unstable and the standard errors for the coefficients mildly inflated making these coefficients significantly not different from zero.

The variance inflation factor (VIF) and tolerance level are commonly used for assessing multicollinearity problems. The VIF shows the degree to which each independent variable is explained by other independent variables. As a rule of thumb, VIF greater than 10 and tolerance level greater than 1 indicates the presence of harmful multicollinearity (Gujarati, 2003). Overall, it can be concluded that looking at the magnitude of the correlation coefficient and considering the VIF and tolerance which are less than 10 in all the cases as shown in Table 4.3, there are no cases of fatal multicollinearity. All the variables in the model are therefore significant with respect to their individual p-values which less than 0.05 which can be explained by strong correlation between the independent variables.

Therefore, table 4.3c/4.4c represents multicollinearity test among the explanatory variables as a way of eliminating any collinearity between two or more variables which may cause error in the regression model.

4.2.3 Regression Analysis

The study used a panel data regression analysis to establishthe relationship between corporate governance and firms' performance. Regression analysis was presented in two ways; the first one using Return on Assets and the second using return on Equityas performance indicators.

Return on Assets (ROA) as a Performance Indicator

From Table , the p-value is 0.000 which indicates that cooperate governance of the firms listed at NSE has influence on their performance. This is because the p-value is less than 0.01 test significance value. Further, the values of the coefficients were found to be significant for all the variables as shown in Table 4.3 below.

Table 3a: Summary of the Regression Model for ROA

Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.561[a]	.315	.305	.1284699

a. Predictors: (Constant), Board Size , CEO Duality , Board Tenure , Board Independence , multiple directorship

Table 3b: ANOVA of Regression Model for ROA

ANOVA

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	2.609	5	.522	31.611	.000[b]
	Residual	5.678	344	.017		
	Total	8.286	349			

a. Dependent Variable: ROA

b. Predictors: (Constant), Board Size , CEO Duality , Board Tenure , Board Independence , multiple directorship

Table 3c: Coefficients of Regression Model for ROA

Coefficients

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.	Collinearity Statistics	
		B	Std. Error	Beta			Tolerance	VIF
1	(Constant)	-.155	.027		-5.807	.000		
	Board Independence	.205	.035	.298	5.922	.000	.786	1.272
	multiple directorship	.009	.002	.237	4.500	.000	.717	1.396
	CEO Duality	.056	.025	.102	2.258	.025	.984	1.017
	Board Tenure	.016	.004	.201	4.103	.000	.833	1.200
	Board Size	-.001	.002	.025	-.503	.615	.824	1.214

a. Dependent Variable: ROA

Y=-0.155+0.205(Board Independence) +0.009(Multiple Directorship) +0.056(CEO Duality) +0.016 (Board Tenure) + -0.001(Board Size).

From the regression results above, the R value was 0.561. This indicates that there was a positive relationship between corporate governance and firm performance of companies listed in NSE. The coefficient of determination also called the R^2 was 0.315. This means that corporate governance explains 31.5% of return on assets of the companies listed in NSE.The remaining 68.50% can be explained using other determinants. The F value of 31.611is significant at a significance value of 0.000 which is less than 0.05 at 5% level of significance. This shows that the overall model of the effects of corporate governance on firms' performance of companies listed in the NSE, Kenya was significant.There is a positive relationship between board independence, , board tenure, CEO duality multiple directorship and firms' performance of companies listed in the NSE, Kenya as supported by beta coefficients of 0.205, -0.001, 0.016, 0.056 and 0.009 respectively. However, there is a negative relationship between board size and firms' performance of companies listed in the NSE, Kenya as supported by beta coefficients of-0.001. This means that an increase in corporate governance will positively increase the firms' performance of companies listed in the NSE, Kenya. The analysis also yields results that show

that corporate governance is statistically significant as the probability (p) value was 0.000 which is not more than the conventional value of 0.05.

According to the regression equation established, taking all factors into account (board independence, board size, board tenure, CEO duality multiple directorship) constant at zero, the firms' performance of companies listed in the NSE, Kenya -0.155. The data findings analyzed also shows that taking all other independent variables at zero, a unit increase in board independence leads to a 0.205 increase in the firms' performance of companies listed in the NSE; a unit increase in board size leads to a -0.001 increase in firms' performance of companies listed in the NSE; a unit increase in multiple directorship leads to a 0.009 increase in the firms' performance of companies listed in the NSE;a unit increase in CEO duality leads to a 0.056 increase in firms' performance of companies listed in the NSE and a unit increase in board tenure leads to a 0.016 increase in firms' performance of companies listed in the NSE. This infers that board independence contribute more to a unit increase infirms' performance of companies listed in the NSE followed by CEO duality, board tenure, multiple directorship, and lastly board size.

4.4.4 Hypothesis Testing

In order to achieve the research objectives, the following five objectives were tested to find out if there exists a statistically significant relationship between corporate governance and firm performance of listed firms in NSE, Kenya. Table 4.5 below presents the summary of result of the test of the hypothesis.

Table 4: Summary of Hypothesis Test

Hypothesis	**Corporate Governance Proxy**	**ROA**	**Conclusion**
		Coefficient (β)	
$H0_1$	Board Independence (BI)	0.205	Reject
$H0_2$	Board size (BZ)	-0.001	Reject
$H0_3$	CEO Duality (CEOD)	0.056	Reject
$H0_4$	Board Tenure (BT)	0.016	Reject
$H0_5$	Multiple Directorship (MD)	0.009	Reject

From the results indicated above, the beta coefficient of all the independent variables were above zero but less than 1 with significance on the dependent variable.

$H0_1$: There is no significant effect of board independence on firms' performance.

The coefficient for board independence is 0.205 for the first model (ROA), implying that it positively affects return on assets further positively. This shows that in all the cases firm performance are affected by board independence. Reject the null hypothesis.

$H0_2$: There is no significant effect of Board size on firms' performance.

On the effect of board size on performance, the coefficients were -0.001 using return on assets as the performance indicator respectively. This implies that, board size affects the performance negatively; consequently, the null hypothesis is rejected.

$H0_3$: There is no significant effect of board tenure on firms' performance.

Board tenure has a coefficient of 0.016. This implies that board tenure positively affects ROA, which is the performance of a firm. Consequently, the null hypothesis is rejected.

$H0_4$: There is no significant effect of CEO Duality on firms' performance.

CEO Duality was found to have coefficients of 0.056. This shows that the model has a positive impact on the performance of an institution. Therefore, the two models lead to rejecting of the null hypothesis.

$H0_5$: There is no significant effect of multiple directorships on firms' performance

Multiple directorships have a positive effect on return on assets as shown by a coefficient of 0.008 and 0.009. Therefore, null hypothesis was rejected.

This shows that corporate governance affects the performance of institutions listed in Nairobi stock exchange.

5.0 SUMMARY OF FINDING, CONCLUSION AND RECOMMENDATION

5.1 Summary of Findings

This objective of the study was to establish the effect of corporate governance on firm's performance of companies listed in the NSE, Kenya. The study found out that all the corporate governance proxies affect firm performance (return on assets) in one way or another. Board size is seen to be corporate governance proxy that has an inverse relationship return on assets.

The study hypothesized that board size, board tenure, CEO duality and multiple directorships affected listed company's performance. Results of the study revealed that on average there were nine board members among all listed companies. The average board independence was 47.4%. Regarding multiple directorship 7 of board members were serving in more than one board and the CEO duality was rated at 9.0%. Most of the board had tenure of 6 years. Generally, listed companies had an average return on assets of 9.0% and return on equity of 13.0%.

Both correlation and regression analysis were used to show the strength and nature of the relationship between corporate governance and firm performance. The first objective of the study hypothesized that board independence had no significant effect on firm performance among listed companies. The study found that board independence had a positive and significant

relationship with firm performance operationalized as return on equity as supported by p value of 0.000 and beta coefficient of 0.205. The results of the study were in contrast with (Bhagat and Black, 2002) who found no significant relationship between board independence and firm performance. These results supported (Weisbach, 2002; John &Senbet, 1998) who found a positive and significant relationship. They posited on the need to increase the number of independent directors since a board composed by professional and outside directors can be in a position to plan and monitor the implementation of company policies. Further, the results are in support of stewardship theory which purports that an organization ought to benefit fully from the composition of skills which can be provided by its board members.

Secondly the study found negative and insignificant relationship between firm performance and board size. The study found that board size had a negative and significant relationship with firm performance operationalized as return on assets as supported by p value of 0.000 and beta coefficient of -0.001. The results were in agreement with Yermack (1996) who found a positive and significant relationship between board size and firm performance. Since the board of directors are mainly involved in planning and monitoring of company policies as compared to management who are involved in day to day running of companies. There are chances of conflict of interest between the two parties which may influence firm performance in an inverse direction as board size increases.

Thirdly there was a positive and significant relationship between CEO duality and firm performance (ROA) as supported by p value of 0.000 and beta coefficient of 0.056 and 0.031 respectively. These results were in disagreement with (Baysinger and Hoskisson, 1997), who argued that CEO duality can be detrimental to a corporate organization the examiner will sit for the same examination thus promoting the need to separate the two. If separated there will be increased board monitoring and availability of advisory services to CEO, from the board chair person.

The fourth objective of the study hypothesized that there was no significant relationship between board tenure and firm performance. The study found positive and significant relationship between board tenure and firm performance (ROA,) as supported by p value of 0.000 and beta coefficient of 0.016 and 0.015 respectively. The results were in agreement with (Bebchuk& Cohen, 2005), who found that board tenure influence the corporate valuation of listed companies. This was mainly supported by increased knowledge effectiveness among board members.

The fifth hypothesis of the study stated that multiple directorship has no significant relationship with firm performance. The study found a positive and significant relationship between multiple directorship and firm performance (ROA) as supported by p value of 0.000 and beta coefficient of 0.009 and 0.008 respectively. The results of the study were in agreement with Gilson (1990) who found a positive and significant relationship between multiple directorship and firm performance.

5.2 Conclusion

The study concluded that a positive relationship exist between firms performance, board independence, CEO Duality and multiple directorship. The correlation analysis shows that there is no strong correlation between corporate governance principles and performance and thus necessitated the use of correlation analysis which is more sensitive to smaller causal relationships. The p-values for all the tests were found to be less than 0.05 which implies that the results from the regression models can be used to make statistical inference to the greatest level of accuracy.

Despite an inverse and significant relationship between board size and firm performance there is need for listed companies to match their board size with companies' specific needs. The inverse relationship can be associated with agency cost which may increase as the board size increases.

5.3 Recommendations

Based on the findings of this research, a number of recommendations can be made to the stakeholders in this field of corporate governance vis-à-vis the performance of an institution. There is need to improve those corporate governance features which have positive impact on firm performance such as CEO Duality and board independence while discouraging those features which have negative impact on corporate governance should be discouraged. Further, Proponents of multiple directorships should note with caution the negative relationship between multiple directorships and operating performance. This is an indicator that the purpose of board independence which is to discipline management of poorly performing firms or otherwise monitor, then board independence has merit. In order to have proper monitoring by independent directors, firms regulatory bodies should require additional disclosure of financial or personal ties between directors or the organizations they work for and the company or its CEO. By so doing, they will be more completely independent. Also, firms should be allowed to experiment with modest departures from the current norm of a "supermajority independent" board with only one or two inside directors.

There is need to develop steps which should be taken for mandatory compliance with the code of corporate governance. Also, an effective legal framework should be developed that specifies the rights and obligations of a firm, its directors, shareholders, specific disclosure requirements and provide for effective enforcement of the law.

There is also the need to set up a unified corporate body saddled with the responsibility of collecting and collating corporate governance related data and constructing the relevant indices to facilitate corporate governance research in Kenya.Finally to the world of academia, there is need for further studies to carry out similar study for a longer time period. A similar study should also be carried out on relationship between firms' performance and corporate governance in MFIs in Kenya.

5.4 Limitations

During the research process, there were a number of challenges which in one way or another affected the process. During literature review, there was enormous literature in this particular field which took quite some time to analyze and identify the appropriate literature. The data collection was also affected by the confidentiality of the information required and the fact that the data was collected through secondary means in consultation with a third part, Nairobi Stock Exchange (NSE) and Capital Markets Authority (CMA) which necessitated the use of numerous reminders and follow ups to persuade the agencies to provide information which took long time because of bureaucracies which were followed.

There was a constraint of time throughout the research process, especially literature review and data collection. Nevertheless these constraints were mitigated by timely programming of activities and avoidance of procrastination of any of the activities. This therefore led to the success and timely completion of the study meeting all the research objectives and aims.

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