Journal of International Business, Innovation and Strategic Management
Vol 1 Issue (5), 39- 61
ISSN: 2617-1805 (Print)

Effect of Corporate Governance on Financial Performance of Companies Listed at Nairobi Securities Exchange, Kenya

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To cite this article:

Kenge, J. (2018). Effect of Corporate Governance on Financial Performance of Companies Listed at Nairobi Securities Exchange, Kenya, *Journal of International Business, Innovation and Strategic Management*, 1(5), 39 – 61

Abstract: The main objective of this study was to establish the effect of corporate governance on financial performance of companies listed at Nairobi Securities Exchange. Specifically, the study examined the composition of board members, shareholders, board size and CEO (Chief Executive Officer) duality has an effect on financial performance of companies listed at the Nairobi Securities Exchange. The study population consisted of all the sixty-six companies that are listed at Nairobi Securities Exchange as at December 2016. The sample population was thirty-five companies listed at NSE. From the multivariate regression analysis, the study established that corporate governance practices such as board composition negatively and significantly affects the financial performance while board size and CEO duality has a positive effect on the financial performance while shareholding has a positive and insignificant effect financial performance of companies listed at the Nairobi Securities Exchange. The study established the existence of significant relationship between corporate governance and financial performance of companies listed at the Nairobi Securities Exchange. The study established that shareholding (ownership concentration) has insignificant effect on financial performance of companies. The study also established that CEO duality and board size positively influences the performance of companies. The study further established that board composition has a negative influence on the financial performance of companies. The study recommends the companies to ensure there is a good balance between the non-executive members and executive members in their boards to ensure the level of their autonomy is high. Further, the study recommends that the chief executive officers especially in a case where the owner doubles up as a chairperson and as a CEO to continue serving in various roles in a company. The study further recommends companies to encourage large shareholders to invest more as they have tendency for monitoring, controlling and ratifying roles in the company. This can improve the performance of the company especially when some of the shareholders are managers.

Key Words: *Board Composition, Ownership Concentration, Board Size, CEO Duality, Financial Performance*

Introduction

Corporate governance in broad terms refers to the processes, mechanisms and relations by which a company is controlled and directed; balancing the multiple interests of stakeholders of a corporation. Corporate governance refers to the processes and structure used to direct and manage business affairs of a company towards enhancing prosperity and corporate accounting with the ultimate objective of realizing shareholder long-term value while taking into account the interest of the other stakeholders (CMA, 2002). Corporate governance is basically concerned with ways in which all parties interested in the wellbeing of the firm (the stakeholders) attempts to ensure that managers and other outsiders are always taking appropriate measures or adopt mechanisms that safeguard the interests of stakeholders. Such measures are necessitated because of separation of ownership from management, an increasingly vital feature of modern corporations (Mwangi, 2013).

Corporate governance is the system by which organizations are directed and controlled. It's a set of relationships between company directors, shareholders and other stakeholders as it addresses the powers of directors and of controlling shareholders over minority interest, the rights of employees, rights of creditors and other stakeholders (Muriithi, 2009). Corporate governance is anchored on different theories that include Agency theory (Jensen and Meckling, 1976) which is most dominant and identifies agency relationship where one party (principal) engages another party (agent) to undertake services on their behalf, Stewardship theory (Donaldson and Davis, 1991) assumes that managers are seen as the best stewards for the organization as they work in the best interest of their principals ; Stakeholder theory (Maher and Anderson, 1999) which states that there is an "exchange relationship" in which organizations should socially responsible and act in best interest of its stakeholders and the 'Nexus of Contracts' Theory.

Solomon (2007) states that we are in a climate change with corporate governance at the centre of this transformation. Not only is there a world wide effort to improve corporate governance, but even countries that have been long-term communist states, such as China and Russia, are embracing a market oriented system with shareholder accountability and greater corporate transparency. Capitalism has survived into the 21st century and seems to be becoming the dominant system in corporate governance. Corporate governance reforms have focused on the sources of system failure and their inability to effectively mitigate the full spectrum of company risks: financial, operational and corruption. Corporate governance has witnessed exponential growth in recent years thus international bodies like Organization for Economic Development (OECD) has developed internationally accepted standards for improvements in corporate governance practices. Almost all the OECD nations are currently revising their corporate governance practices or have recently done so (OECD, 2003).

When corporate governance is weak and the checks and balances are ineffective, then a company is bound to collapse. For instance, Solomon (2007) noted that corporate governance in Enron was weak in almost all aspects. The board of directors was composed of a number of people who had been shown to be of poor moral character and willing to conduct fraudulent activity. This was the genuine root of the company's corporate governance failure. Also, the non- executive directors were compromised by conflicts of interest. The internal audit committee did not perform its function of internal control and of checking the external auditing function. Furthermore, the company's accounting and financial reporting function failed miserably. Both the financial directors and the chief executive were prepared to produce fraudulent accounts for the company.

Good corporate governance practices are thus necessary for any company to operate effectively in both the local and global market. Developing countries are increasingly embracing the concept of good corporate governance knowing it leads to sustainable growth. Indeed corporate governance in Kenya is gaining some level of recognition with very little work in the area even in the well regulated institutions. Corporate governance and financial performance go hand in hand in that a company that has good corporate governance practices is likely to perform better than a company that has poor corporate governance practices. Several studies have been done to establish the effect of corporate governance on firm’s performance. Sanda et al (2005) argued that a strong corporate governance structure, could lead to higher performance.

Statement of the Problem

The practice of corporate governance that is being depicted in organizations both locally and internationally is crucial as it enhances good performance and the reputation of any given organization. Poor corporate governance practices are unhealthy to an organization in that such practices could either lead to poor performance of a company or even lead to total closure as such organizations cannot get to sustain their daily operations or due to the bad reputation it has, thus most stakeholders tend to shy away from it in fear of incurring losses. Thus, corporate governance is very crucial in each and every organization regardless of the industry, the size and the growth of any given organization. The practice of good corporate governance has therefore become a necessary prerequisite for any corporation to be managed effectively in the global market (Mwangi, 2013). According to Mang’unyi (2011) previous researchers have been only concentrating on the banking and other service industries thereby ignoring other sectors like automobile sectors that also contribute to the Kenyan economy and are also prone to corporate governance issues like the automobiles industry, commercials and services and others. For instance at the CMC motors Kenya there were revelations that some members of the board of directors had been fleecing the company and stashing the loot in foreign accounts and also the current corruption scandals at the National Youth Service (NYS) where millions of shillings got stolen.

According to Muriithi (2009), many companies have been characterized by scandals. This is so because of lack of sound corporate governance that has led to poor performance of organizations all over the world and also suppressing sound and sustainable economic decisions. Some Kenyan financial institutions like Dubai bank, Imperial bank and Chase bank were put under receivership due to inappropriate corporate governance practices.

A number of studies have been done at the local level on corporate governance and financial performance. For instance, Muriithi (2005) did a study on the relationship between corporate governance mechanisms and performance of firms quoted on the Nairobi Stocks Exchange, Matengo (2008) did a study on the relationship between corporate governance practices and performance of banking industries in Kenya while Mwangi (2013) conducted a research on the effect of corporate governance on financial performance of companies listed at Nairobi Securities Exchange. Although more and more research is being done on corporate governance, relevant data from empirical studies are still few, thus limiting the in depth understanding of corporate governance concerns. With such surrounding environment and perpetrators of unethical acts in organizations being left without proper actions being taken against them, the interests of minority stakeholders could be compromised thus no research has been done on all sectors of companies as previous researchers have been concentrating on the financial sector and ignoring others like the automobiles industry like CMC motors and NYS that faced corporate governance scandals.

Objectives of the Study

i. To examine the effect of board composition on the financial performance of companies listed at NSE.
ii. To establish the effect of ownership concentration on the financial performance of companies listed at NSE.
iii. To establish the effect of board size on the financial performance of companies listed at NSE.
iv. To find out the effect of CEO (Chief Executive Officer) duality on the financial performance of companies listed at NSE.

Literature Review

Theoretical Review

Agency Theory

It is acknowledged that the principal agent theory is generally considered the starting point for any debate on the issue of corporate governance emanating from the classical thesis on The Modern Corporation and Private Property by Berle and Means (1932). Agency theory describes the financial-economic relationship that arises between the principal (shareholder) and the agent (management). Jensen and Meckling (1976) define the agency relationship as a contract under which one party (the principal) engages another party (the agent) to perform some services on their behalf. As part of this, the principal will delegate some decision making authority to the agent. The problem that arises as a result of the type of corporate ownership system is that agents do not necessarily make decisions in the best interest of the principals. It is likely that the company managers prefer to pursue their own personal objectives such as aiming to gain the highest bonuses possible. Managers are likely to display a tendency towards `egoism' (i.e., behavior that leads them to maximize their own perceived self-interest: Boatright, 1999). This can result in a tendency to focus on the project and company investments that provide high short run profits (where managers' pay is related to this variable), rather than maximization of long-term shareholder wealth through investment in projects that are long-term in nature (Solomon, 2007).

Agency theory suggests that there are several mechanisms to reduce the agency problem in a company. For instance, establishing a `nexus' of optimal contracts (both explicit and implicit) between the company management and shareholders that include remuneration contracts for management and debt contracts; shareholder activism through voting at AGMs, takeover mechanisms, passing of shareholder resolutions where a group of shareholders together lobby the company on issues with which they are dissatisfied and divesting (selling their shares); and finally threat of firing. This theory is relevant to this study in that it informs about the board characteristics which is the independent variable. Board members are agents of a firm thus are expected to keep at hand the interests of the firm rather than focusing on their own selfish gains.

Stewardship Theory

This theory is anchored on the premise that directors will fulfill their duties towards the shareholders. The directors are the stewards whose motives are aligned with the objectives of the principles. Donaldson and Davis (1991) states that stewardship theory assumes managers are stewards whose behaviors' are aligned with the objectives of their principals. Davis, schoorman & Donaldson (1997) defined a steward as one who protects and maximizes shareholders wealth through firm performance, because by doing so, the steward's utility functions are maximized. In this theory, the directors protect the shareholders interests and make decisions on their behalf. The main objective of the directors is to form and maintain successful companies for shareholders to prosper. This theory is relevant to this study as it informs about the board characteristics which is the dependent variable. The board members/directors are stewards who are expected to uphold the interests of the firm wholly on behalf of the shareholders.

Stakeholder Theory

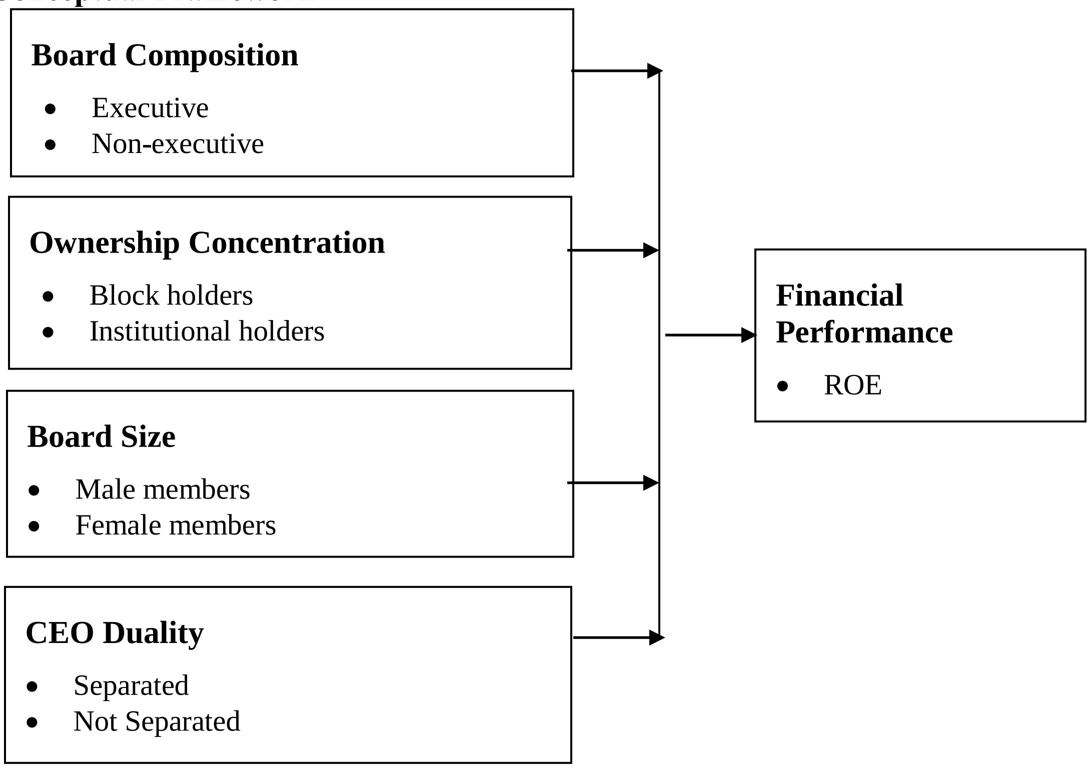
Stakeholder theory may be viewed as a conceptual cocktail, concocted from a variety of disciplines and producing a blend of appealing sociological and organizational flavors. Indeed, stakeholder `theory' is less of a formal unified theory and more of a broad research tradition, incorporating philosophy, ethics, political theory, economics, law and organizational social science (Wheeler et al.,2002). Stakeholder theory can be defined in different ways and `stakeholder', depending on the user's disciplinary perspective. One commonality characterizing all definitions of stakeholders is to acknowledge their involvement in an `exchange' relationship (Pearce, 1982; Freeman, 1984; Hill and Jones, 1992). Stakeholders are not only affected by a firm but they also affect the firm in some way. Solomon (2007) noted that stakeholders include shareholders, employees, suppliers, customers, creditors, communities in the vicinity of a company's operations and the general public. The most extreme of proponents of stakeholder theory suggest that the environment, animal species and future generations should be included as stakeholders. Indeed, the stakeholder relationship has been described as one of exchange where the stakeholder groups supply companies with `contributions' and expect their own interests to be satisfied via `inducements' (March and Simon, 1958).

The 'Nexus of Contracts' Theory

Bloomfield (2013) states that the theory recognizes the essential contribution of the principal-agent arrangement in identifying the separation between ownership and control of the company but goes onto regard the firm as a junction of all activities it undertakes with the co-ordination of traffic through this junction undertaken by managers. The company becomes a 'nexus of contracts' – a series of relationships often backed by legal agreements, which are constantly fluid, occupy ever-changing priorities and compete for resources: company-customers; company-suppliers; company-employees; company-state; company-competitors even. In this respect the nexus theory draws on a body of social and political theory from the social contractualists like Hobbes, Locke and Rousseau, as well as the anti-contractualists like Marx and modernists like Rawls and Nozick. The theory suggests that the driving force behind all this constant change is the economic concept of self-maximizing the utility of all the parties and, not least, of the managers. In a nutshell, the theory deals with the governing structure and the processes in an organization.

Journal Of International Business, Innovation and Strategic Management
Volume 1, Issue 5, 2018, ISSN: 2617-1805 (Print)

Conceptual Framework



Independent Variables **Dependent variable**

Figure 1 Conceptual Framework

Board Composition

Boards mostly compose of executive and non-executive directors. Executive directors refer to dependent directors and non-executive directors to independent directors (Shah et al., 2011). From an agency theory perspective, non-executive directors may be perceived as playing a monitoring role on the board. There is a substantial quantity of academic literature indicating that board of directors perform an important corporate governance function and that non-executive directors act as necessary monitors of management (e.g., Fama,1980; Fama and Jensen,1983). Without the monitoring function of non-executive directors it would be more likely that inside executive directors would be able to manipulate their position by gaining complete control over their own remuneration packages and securing their jobs (Morck et al., 1988). The presence of outsiders on company board is thought to be positively related to corporate control activity, as outsiders can facilitate takeovers, thereby activating the takeover constraint that disciplines company management, (Agrawal & Knoeber, 1996).

The greater emphasis on diversity was seen as one of the changing features of boards. People commented on the need for diversity not only in the sense of gender or ethnic background, but for a generally broader balance. This included people with different geographical experience, and a desire to get genuinely independent views from people with different industry backgrounds. Search criteria now included looking for more functional skills, such as strategy, human resource, or IT skills. It was noted that historically non-executives were brought on in part to introduce new business or facilitate contacts; this still occurred in some cases where people were recruited who had a deep understanding of a particular business segment. This had implications not only for helping understand how buying decisions are made, but to also help understand upcoming product requirements in a particular industry segment (Smerdon, 2010)

Ownership Concentration

The modern firms face the problem of having to separate ownership and control, thus it's critical to monitor the management to ensure it acts in shareholders' interest. Though the biggest and block shareholders have got the resources and incentives to monitor the managements work, a dispersed shareholding structure suffers from ``free rider'' problem. In general, the corporate governance literature has identified block ownership as an influential mechanism that mitigates the agency problem between managers and shareholders (Shleifer and Vishny, 1997 and Claessens and Djanklov, 1999). Large shareholders provide at least a partial solution to the free-rider problem of small investors, but block holders ownership above a certain level may lead to the entrenchment of owner-managers that expropriate the wealth of minority shareholders (Fama and Jensen, 1983, Morck et al., 1989 and Shleifer and Vishny, 1997).

Board Size

The Board of Directors of any given company is a key mechanism to monitor the 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 their 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). Hermalin & Werisbach (2003) argued the possibility that larger boards can be less effective than small boards. When boards consist of too many members agency problems may increase, as some directors may lag along as free-riders. They argue that when a board becomes too big, it often moves into a more symbolic role, rather than fulfilling its intended function as part of the management.

Dalton & Dalton (2005) on the other hand argued that very small boards lack the advantage of having the spread of expert advice and opinion around the table that is found in large boards. Furthermore, larger boards are more likely to be associated with an increase in board diversity in terms of experience, skills, gender and nationality.

CEO Duality

According to the academic literature, separating the role of the chairman and the chief executive is a corporate governance initiative that can reduce agency problems and result in improved corporate performance because of more independent decision making (Donaldson & Davies, 1994). Agency problems get reduced by mechanisms that aid in monitoring of boards so as to align shareholder and management interest. Some studies have shown that splitting the role has indeed led to significantly higher financial performance (Peel & O'Donnell, 1995). However, it has been suggested that such improvements may be a case of wishful thinking and that the evidence is not persuasive enough to engender splitting the roles in practice (Daily & Dalton, 1997). The roles of chairman and chief executive should not be exercised by the same individual.

(Suggested revisions to the Combined Code, 1998, Annex A of the Higgs Report, 2003)

On the other hand, Westphal (1999) reported that social ties between the CEO and the board enhance the provision of advice and counsel from outside members of the board on important strategic issues. CEOs, it seems, are more likely to seek advice when they feel they can rely on the loyalty of members of the board as reflected in social ties. A decision to combine the posts of chairman and chief executive officer in one person should be publicly justified (The Combined Code, 1998).

Research Methodology

The study employed a descriptive research design that was carried out as a survey of 66 companies listed at NSE as at December 2016. The population of the study consists of 66 financial and non-financial firms listed on the Nairobi Securities Exchange as at 31st December 2016. A sample size of 35 firms was used for the study. This represented 53% of the target population was acceptable according to an argument by Mugenda and Mugenda (2008). Secondary data spanning 5 years (2012 to 2016) was used in the study to achieve the objectives. Both descriptive and inferential analysis was conducted on the data set. Diagnostic tests of normality of the dependent variable and multicollinearity test were conducted before running an ordinary least square regression model. The following multivariate linear regression model was tested. $Y= \beta_0+ \beta_1X_1+\beta_2X_2+ \beta_3X_3+ \beta_4X_4 + \varepsilon$Where: Y is the dependent variable (Financial Performance), X_1 is Board Composition, X_2 is Ownership Concentration, X_3 is Board Size, X_4 is CEO Duality, β_0 is the regression constant, β_1, β_2, $\beta_{3,}$ and β_4 are the regression coefficients and ε is the error term.

Results

Descriptive Analysis

Descriptive statistics were carried out to establish the measures of fundamental trend of the study variables. The study used minimum and maximum values, mean and standard deviation to provide the descriptive for the variables of the study. The results are as illustrated in Table 1.

Table 1 Descriptive Statistics of the Variables

Company	Minimum	Maximum	Mean	Standard Deviation
Board Composition	0.6	12	4.78	3.0913351
Board Size	5	18	10.3714	4.1874
CEO Duality	0	1	0.5429	0.5054
Ownership Concentration	0.29	0.57	0.4217	0.0746
ROE	-32.64	33.69	3.7928	15.5552

The findings of the study indicated that that the company with the minimum ratio of board composition (ratio of executive to non-executive) had 0.6 while that with maximum ratio had 12. Though, on average the most companies had board composition ratios of 5 as shown by the mean of 4.78. The results also indicated that most of the listed companies had a board size of 10 members with that with maximum number having 18 while that with the least number having 5 as shown in table 1. These results reveals that majority of these companies have a bloated board size. Moreover, the results of the study showed that most of the chief executive officers of the listed companies had CEOs holding dual roles as indicated by a mean of 0.54. In addition, the results of the study showed that most the shareholders of listed firms have a minimum ownership concentration of 0.29 while those with the maximum had 0.57. The findings indicate that most of these companies have block shareholders with ownership concentration value of 0.4 as shown by a mean of 0.4217.

Analysis of Board Composition and Financial Performance

The study asked the respondents to indicate the number of males and females in their board. The findings of the study showed that majority of the board members are male (68%) while the female board members were 34%. The results of the study indicate that the gender of the board composition complies with the Kenya 2010 constitutions' two third gender rule.

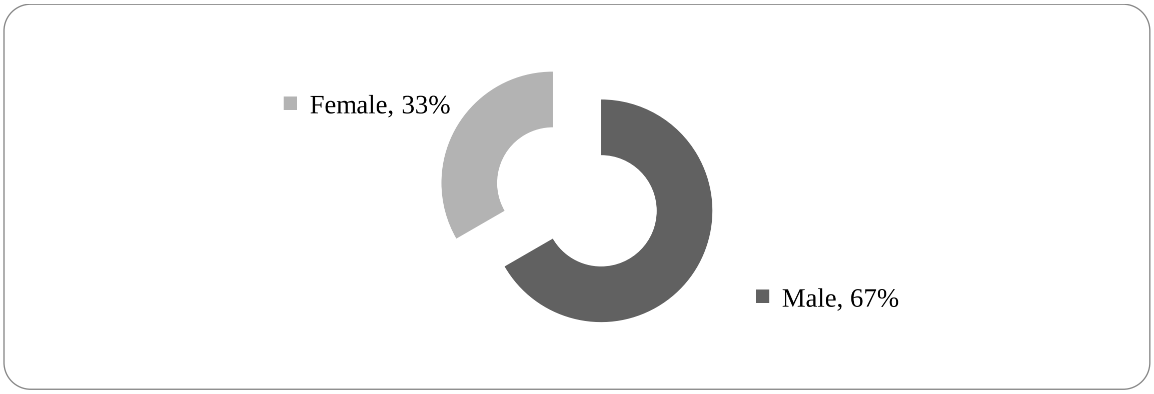


Figure 2 Gender of the Board Composition

The study also sought to determine the number of executive and non-executive directors in the board. The results of the study revealed that majority (78.6%) of the board are comprised of executives while only 21.4% are non-executive. This is because the majority of the board's decisions are made by the executive directors.

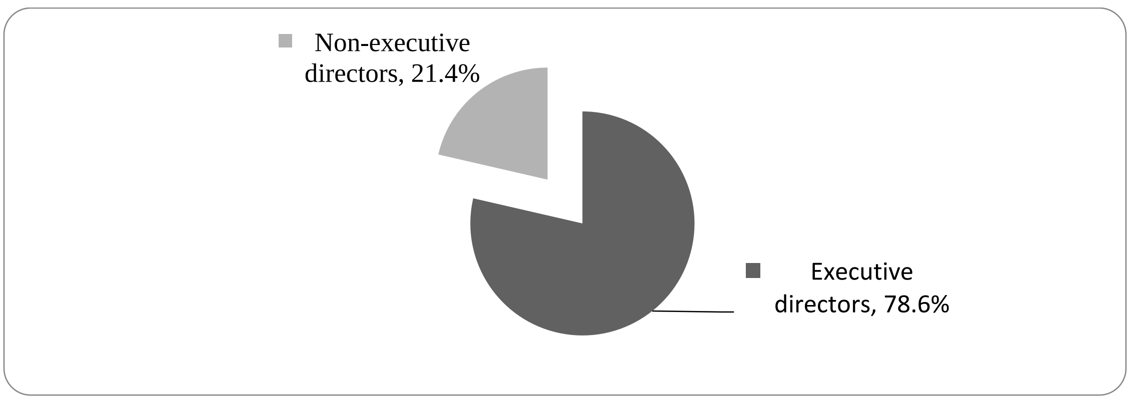


Figure 3 Number of Executive and Non-Executive Directors

The study sought to establish the trend in board composition and financial performance of selected companies listed at NSE. The results are presented in figure 4.

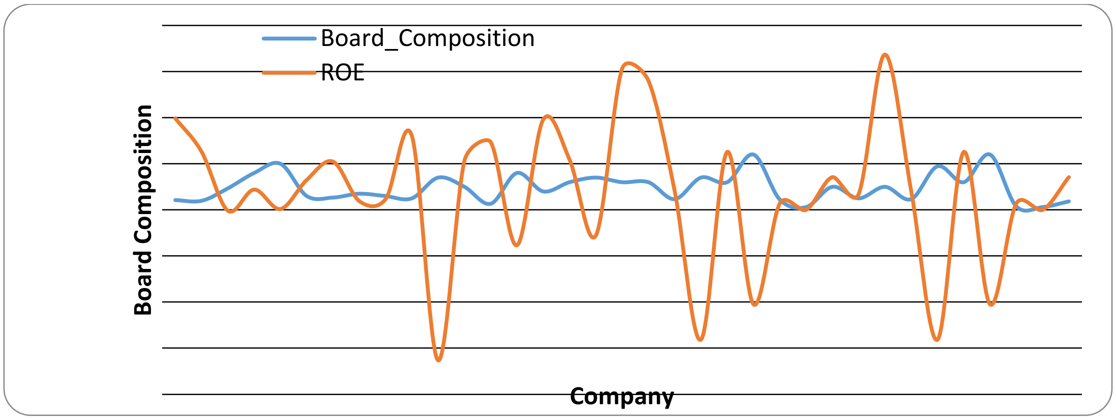


Figure 4 Trend Analysis of Board Composition and Financial Performance

The trend results presented in figure 4 indicated the composition of board members for the listed companies vary across. The findings implied that the listed companies at NSE have varying composition of executives to non-executives.

Analysis of Ownership Concentration and Financial Performance

The study sought to determine the ownership concentration of the companies listed at the Nairobi Securities Exchange. The results of the study are presented in Figure 5.

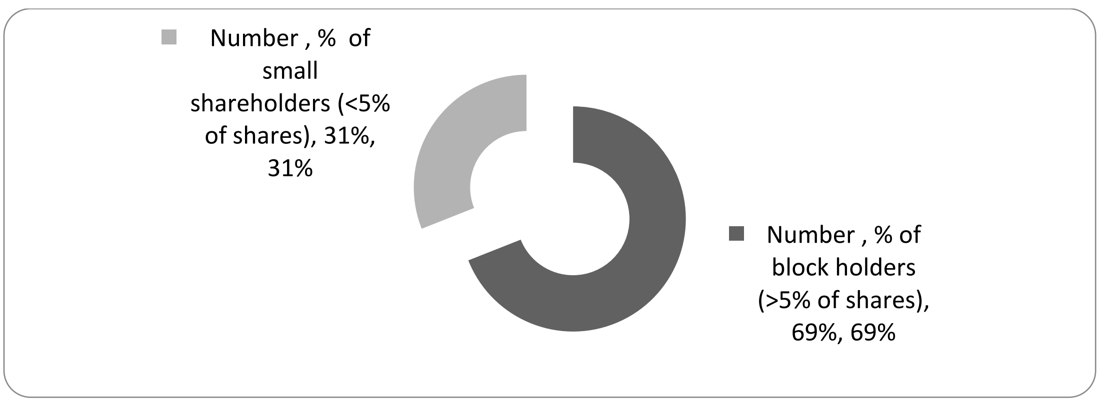


Figure 5 Share Holding/ Ownership Concentration

Moreover, the study sought to determine if there are restrictions on the maximum shares held by one individual or institution in the companies listed at NSE. The results of the study showed that majority of the companies have restrictions on the maximum shares to be held by an individual.

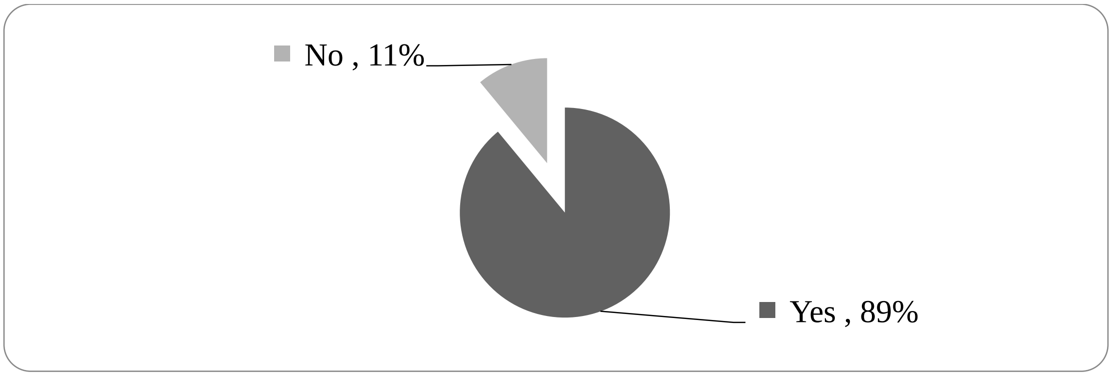


Figure 6 Share Ownership Restrictions

The study also sought to establish the relationship between ownership concentration and financial performance of selected companies listed at NSE. The results presented in figure 7.

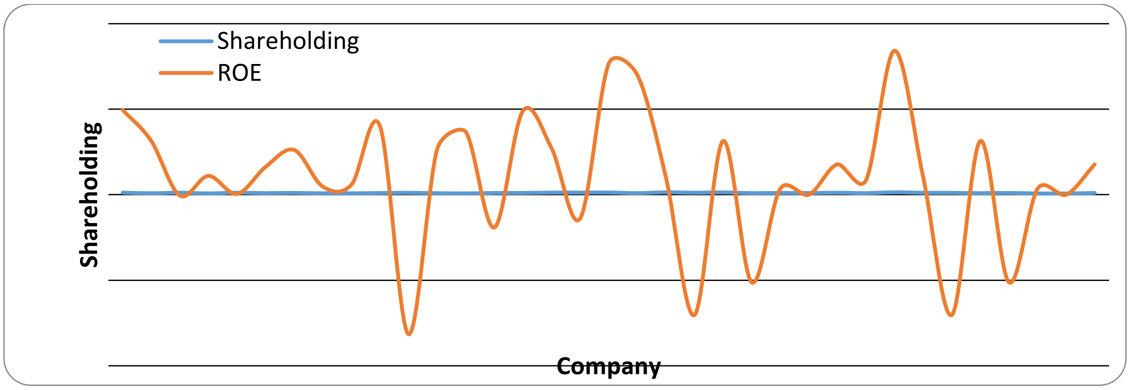


Figure 7 Trend Analysis of Ownership concentration and Financial Performance

The trend result presented in figure 7 reveals that ownership concentration vary from one company to the other. The results indicate that ownership concentration positively influences firm value. On the other hand, the influence of ownership concentration on firm value could be negative, because a highly concentrated ownership.

Analysis of Board Size and Financial Performance

The study sought to determine the average number of board size of companies listed at NSE for the last 5 years between the years 2012 to 2016. The results of the study revealed that the majority of the companies listed at NSE had an average of 8 members in their board in 2012. In 2013, the average board size for every company was 8 members while in 2014 they had an average of 9 members. The results of the study showed that majority of the companies had a board of 10 members in 2015 while in 2016 they had an average of 10 members. The findings of the study indicate that the average number of board members sitting in a company has been increasing.

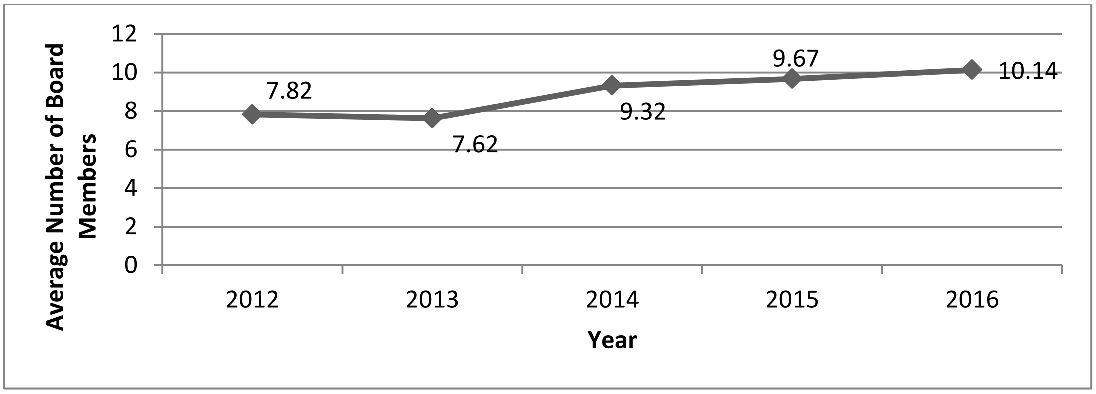


Figure 8 Average Number of Board Size

The study also sought to determine whether there are restrictions in terms of the maximum number of members to sit on a board. The results of the study indicated that all the firms have restrictions on the number of members that sit in a board of companies listed at the NSE. The results of the study are as presented in table 2.

Table 2 Restrictions on the Number of Members to Sit on a Board

Restrictions on members sitting on a board	Percentage (%)
Yes	100
No	0

The study sought to establish trend results on the relationship between the board size and financial performance of companies listed at NSE. The findings presented in figure 9.

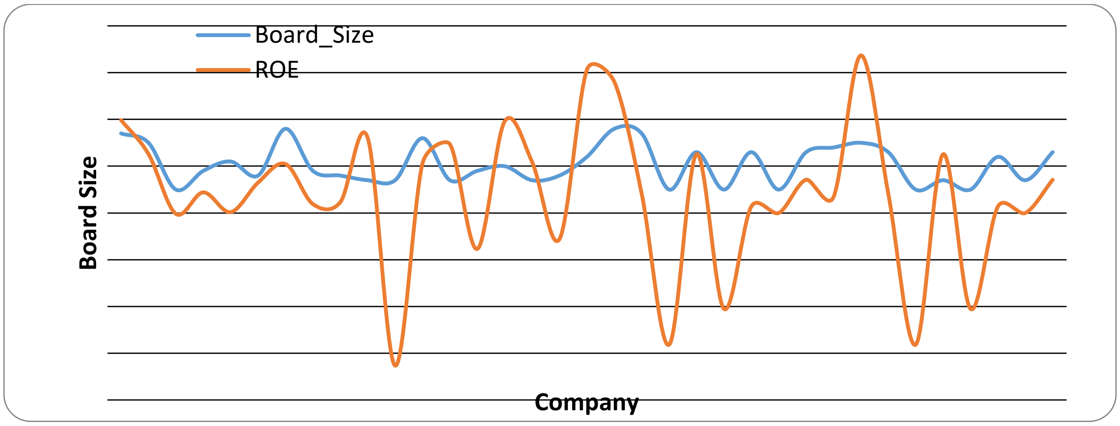


Figure 9 Trend Analysis of Board Size and Financial Performance

The findings presented in figure 9 indicated that the size of the board varied from one company to the other. The results indicate that the companies with larger board size perform poorly financially. This is because board size has a strong negative impact on profitability and share returns.

Analysis of CEO Duality and Financial Performance

The study sought to determine whether there is the separation of the CEO and the board chair or not. The findings of the study revealed that majority (54.3%) of the respondents indicated that there is no separation of the CEO and the board chair while those who indicated that there is separation of the CEO and the board chair were 45.7%. this findings implies that most firm's have one CEO who doubles up as a the board chair.

Journal Of International Business, Innovation and Strategic Management
Volume 1, Issue 5, 2018, ISSN: 2617-1805 (Print)

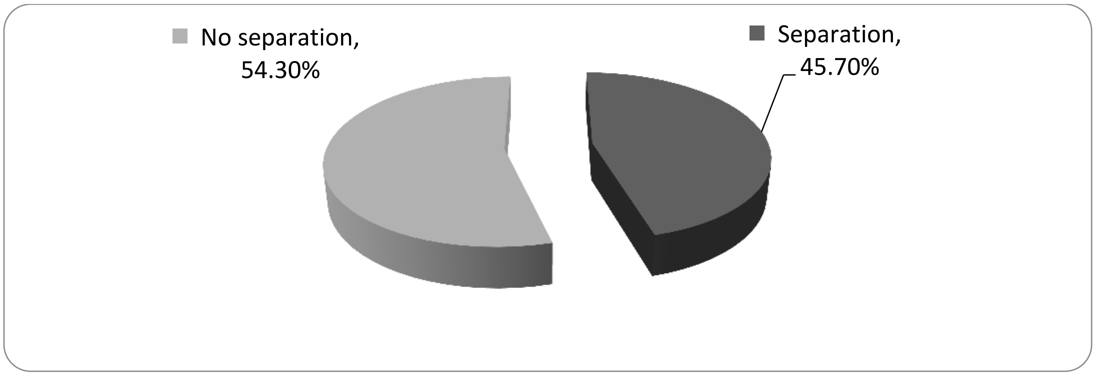


Figure 10 CEO duality

The study sought to examine the connection between CEO Duality and financial performance of companies listed at NSE. The trend results are as presented in figure 11.

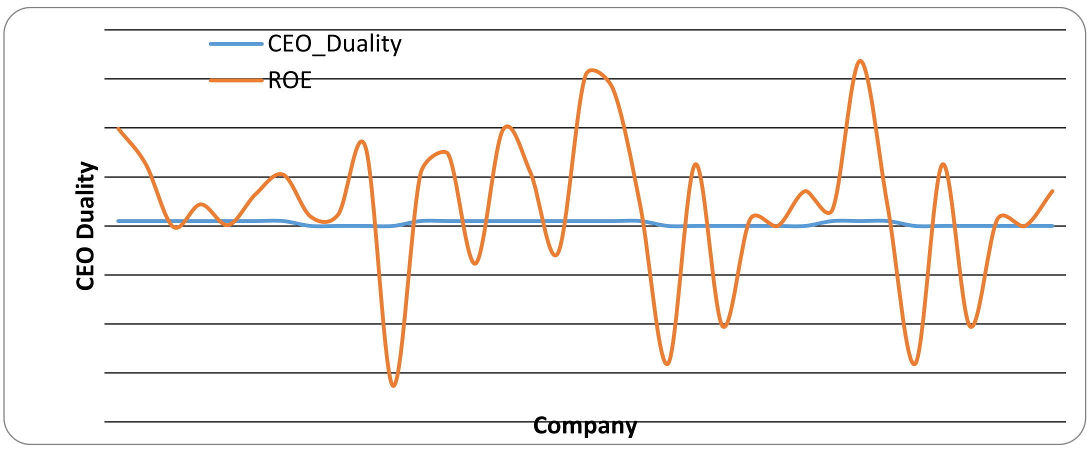


Figure 11 Trend Analysis of CEO Duality and Financial Performance

The trend results in figure 4.13 on CEO Duality of the listed firms shows that the duality of chief executive officers varied from one company to the other. The results further indicate that companies with CEO Duality perform poorly financially. This is because CEO duality has a negative impact on the firm performance.

Correlation Analysis

The study used Pearson correlation to examine the effect of corporate governance on the financial performance of companies listed at the Nairobi Securities Exchange. The findings are presented in table 3.

Table 3 Correlation Matrix Results

Correlations		**Board Composition**	**Board Size**	**CEO Duality**	**ownership concentration**	**ROE**
Board Composition	Pearson Correlation	1				
Board Size	Pearson Correlation	-.353*	1			
CEO Duality	Pearson Correlation	-0.055	.444*	1		
Ownership Concentration	Pearson Correlation	0.248	0.214	0.24	1	
ROE	Pearson Correlation	-.456*	.593*	.480*	0.093	1
	Sig. (2-tailed)	0.006	0.000	0.004	0.597	

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

The findings presented in Table 3 shows that board composition had a negative and significant correlation with the financial performance (ROE) of listed companies at NSE. This was shown by the Pearson Correlation value of -0.456 and p-value of 0.006. This findings implies that an increase in the composition of non-executive to executive board members have negative effect on the financial performance of listed firms. On the other hand, an increase in the ratio of executive to non-executive composition of board members has a positive effect on ROE of a company. The findings of this study agrees with those of VO and Phan (2013) which indicated that elements of corporate governance like the presence of female board members, CEO duality, board members working experience and board compensation have a positive effect on performance of firms, as measured by the return on asset (ROA). Similarly, the findings showed that board size and return on equity of companies listed at Nairobi Securities Exchange had a strong, positive and significant association. This was shown by the Pearson Correlation value of 0.593 and p-value of 0.000. These findings implied that an increase in board size could lead to a increase in financial performance of a company in terms of ROE. This is because a bigger board size translates to a higher monitoring role of the members. The results are in agreement with the findings of a study by Mwangi (2013) which found that a strong relation exists between the corporate governance practices under study and firms financial performance.

Moreover, the study sought to establish the association between CEO Duality and net profits of commercial banks. The correlation results indicated the existence of a positive and significant relationship between CEO Duality and the financial performance of companies listed at the NSE. This was shown by the Pearson Correlation value of 0.480 and p-value of 0.004. These results implied that increasing the number of board meeting leads to increase in the financial performance (ROE) of companies listed at the NSE. These results concur with the results of a study by Baker, Godridge, Gottesman and Morey (2007) reported a significantly positive relation between firm level (and country-level) corporate governance ratings and market valuation, suggesting lower cost of equity for better governed firms. Lastly, the results of the study revealed that ownership concentration has a positive and insignificant effect on the financial performance of companies listed at the Nairobi securities exchange. This is indicated by a Pearson Correlation value of 0.093 and p-value of 0.597. This implies that an increase in the ownership concentration of the stakeholders of companies listed at the Nairobi Securities Exchange have an insignificant effect on ROE of company. The findings are consistent with the findings of a study by Mang'unyi (2011) which revealed that there was a significance difference between corporate governance and financial performance of banks.

Diagnostic Tests

Statistical tests rely upon certain assumptions about the variables used in the analysis. When the assumptions are not met, the results may not be trustworthy resulting into either Type I or Type II error (Osborne *et al*, 2011) or over or under-estimation of significance or effect sizes. The assumptions of the regression analysis are of two kinds: those that are robust to violations and assumptions that are not robust to violations. This study addressed assumptions of multiple regressions that are not robust to violations. Data diagnostic tests such as normality of the dependent variable, Multicollinearity and homogeneity were done to test for statistical assumptions and determine if the data collected was properly modeled. Multicollinearity was assessed in this study using the variance inflation factors (VIF). According to Field (2009) VIF values in excess of 10 is an indication of the presence of Multicollinearity. The results in Table 4 present variance inflation factors results and were established to be less than 10 for all the predictor variables and thus according to Field (2009), it indicates that there is no Multicollinearity in the data collected. It was hence suitable to run a regression model.

Table 4 Variance Inflation Factor Test of Multicollinearity

Variables	**VIF**	**1/VIF**
Board Composition	1.31	0.764558
Ownership Concentration	1.23	0.812079
Board Size	1.14	0.880611
CEO Duality	1.08	0.926855
Mean VIF	**1.19**	

The study also conducted a normality test to find out whether the dependent variable was normally distributed. Saunders (2007) posits that when this assumption is violated, the study results are likely to give biased estimates of the parameters. Kolmogorov-Smirnov and Shapiro-Wilk test were used to test the normality of dependent variable. The findings in Table 5 reveal that the Kolmogorov-Smirnov and Shapiro-Wilk statistics were 0.065 and 0.785 respectively whereas the associated p-value was 0.123 and 0.568 for Kolmogorov-Smirnov and Shapiro-Wilk statistics respectively. Since the p-values for both tests were greater than the $\alpha = 0.05$, the study concluded that the dependent variable is normal in distribution and hence subsequent analysis could be carried out.

Table 5 Kolmogorov-Smirnov Test of Normality

	Kolmogorov-Smirnov[a]			Shapiro-Wilk		
	Statistic	**df**	**Sig.**	**Statistic**	**df**	**Sig.**
Performance of public service delivery	0.065	31	.123	0.785	31	0.568

Multivariate Regression Results

The study finally employed the multivariate regression analysis to test the relationship between the independent variables and the dependent variable. The results presented in table 4.4 indicated that corporate governance practices (board composition, board size, CEO Duality and ownership concentration) jointly accounted for 49.8% (as shown by R-Square =0.498) of the variation in the financial performance of companies listed at the NSE. The findings also revealed that the model was significant (R=0.706).

Table 6 Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.706	0.498	0.431	11.730526

The findings of ANOVA presented in table 7 indicate that the model used to link the predictor variables (corporate governance practices) to the financial performance of the companies listed at the Nairobi Securities Exchange was statistically significant as shown by F-statistics=7.446 and p-value=0.000. These findings implied that board composition; board size, CEO Duality and ownership concentration were significant predictors of financial performance of the companies listed at the Nairobi Securities Exchange.

Table 7 Analysis of Variance (ANOVA)

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	4098.632	4	1024.658	7.446	.000
	Residual	4128.157	30	137.605		
	Total	8226.789	34			

Regression coefficient results were used to examine the effect of each corporate governance practice. The Regression Coefficients Results are presented in table 8 below.

Table 8 Regression Coefficients Results

Predictor Variable	B	Std. Error	Beta	t- statistic	Sig.
(Constant)	-8.886	12.092		-0.735	0.468
Board Composition	-1.65	0.746	-0.328	-2.213	0.035
Board Size	1.246	0.595	0.335	2.093	0.045
CEO Duality	9.422	4.514	0.306	2.087	0.045
Ownership Concentration	5.996	29.781	0.029	0.201	0.842

The findings indicate that board composition had a negative and significant relationship with return on equity (β= -1.65, p=0.035). These findings implied that an increase in board composition would lead to decrease in the financial performance of companies listed at the NSE. The results further implied a unit increase in board composition would results to 1.65 unit decrease in the financial performance of companies listed at the NSE. The findings of this study agrees with those of VO and Phan (2013) which indicated that elements of corporate governance like the presence of female board members, CEO duality, board members working experience and board compensation have a positive effect on performance of firms, as measured by the return on asset (ROA). The study results also showed that board size had a positive and significant association with return on equity (β= 1.246, p=0.045). These findings implies that an increase in board size lead to a positive increase in the financial performance. A unit increase in board size would lead to 1.246 unit decrease in the financial performance of companies listed at the NSE. The results are in agreement with the findings of a study by Mwangi (2013) which found a positive relationship between board size and firms financial performance.

Moreover, the study sought to establish the relationship between the CEO duality and financial performance of companies listed at the NSE. The findings showed that CEO Duality has a positive and significant effect on the financial performance of companies listed at the NSE (β= 9.422, p=0.045). This implies that CEO duality has a positive effect on the company ROE. These results concur with the results of a study by Baker, Godridge, Gottesman and Morey (2007) reported a significantly positive relation between firm level (and country-level) corporate governance ratings and market valuation, suggesting lower cost of equity for better governed firms. Finally, the results of the study indicated that ownership concentration had a positive and insignificant effect on financial performance of companies listed at the NSE (β= 5.996, p=0.842). This implies that an increase in the number of block shareholders in company has positive but not significant effect on the company's return on equity. It means that regardless of whether the ownership is block or not, it has no significant effect on financial performance. The findings are consistent with the findings of a study by Mang'unyi (2011) which revealed that there was a significance difference between corporate governance and financial performance of banks.

Conclusions

The study concludes that board composition has a negative and significant relationship with return on equity of firms listed at NSE, Kenya which shows that an increase in board composition would lead to decrease in the financial performance of companies listed at the NSE. The study concludes that ownership concentration positively and insignificantly affect financial performance of companies listed at the NSE, Kenya which reveals that an increase in the number of block shareholders in company has positive but not significant effect on the company's return on equity.

It was also concluded that board size has a positive and significant association with return on equity which implies that an increase in board size lead to a positive increase in the financial performance. Larger board size enhances diversified opinion on key issues being decided on board which is good for the company. The study also concludes that CEO Duality has a positive and significant effect on the financial performance of companies listed at the NSE, Kenya implying that firms whose CEOs also double up as chairpersons perform well as compared to those whose CEOs don't double up as chairpersons.

Recommendations

The study derived some recommendations to the study based on the findings of the study. The study recommends the companies to ensure there is a good balance between the non-executive members and executive members in their boards to ensure the level of their autonomy is high. This is because a board with a higher composition of executive to non-executive (independence) is effective in carrying out its directive. The study recommends companies to ensure there is transparency, innovation and accountability of their board members so as to enhance their performance. Lack of accountability and transparency in larger boards is likely to affect the performance of companies.

Further, the study recommends that the chief executive officers especially in a case where the owner doubles up as a chairperson and as a CEO to continue serving in various roles in a company. The study further recommends companies to encourage large shareholders to invest more as they have tendency for monitoring, controlling and ratifying roles in the company. This can improve the performance of the company especially when some of the shareholders are managers.

Conflict of Interest

No potential conflict of interest was reported by the authors.

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