EFFECT OF CORPORATE GOVERNANCE PRACTICES ON

FINANCIAL PERFORMANCE OF LISTED AGRICULTURAL FIRMS IN THE

NAIROBI SECURITIES EXCHANGE

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A RESEARCH PROJECT SUBMITTED IN PARTIAL FULFILMENT OF THE

REQUIREMENT FOR THE AWARD OF A MASTER OF BUSINESS

ADMINISTRATION DEGREE, SCHOOL OF BUSINESS, UNIVERSITY OF

NAIROBI.

2017

DECLARATION

This research project is my original work and has not been submitted for examination in any other learning institution.

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ACKNOWLEDGMENTS

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This study is dedicated to my sponsor and my family for being supportive during the time of my studies.

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LIST OF ABBREVIATIONS & ACRONYMS

CMA	Capital Market Authority
CEO	Chief Executive Officer
EPS	Earning per Shares
NSE	Nairobi Securities Exchange
OECD	Organization for Economic Cooperation and Development
PAT	Profit after Tax
PBT	Profit before Tax
ROA	Return on Assets
ROCE	Return on Capital employed
ROE	Return on Equity
SPSS	Statistics Package for Social Sciences

ABSTRACT

The objective of this research was to determine the influence of corporate governance practices on financial performance in listed agricultural companies in Kenya. The corporate governance practices included board of directors' composition and size, independence of board and audit committees. The researcher used a descriptive correlation research design to determine the relationship between corporate governance practices and financial performance. The population comprised of all the seven firms that were listed in the Nairobi Securities Exchange (NSE) in the period 2012-2016. The data set comprised of secondary data collected from annual reports. A multiple regression model of financial performance against corporate governance practices was applied. It was found the R^2 values were sufficiently less than 0.5 for ROA and ROE implying low predictor power while that of debt equity ratio was high that shows that some companies had violated the CMA Act threshold of three directors in the audit committee while other had poor board composition, also breached was benchmark set by the CMA Act for the independence of directors. The study established that corporate governance practices have no significant influence on ROE and ROA of listed agricultural firms in Kenya. However, it had significant influence on debt equity ratio The findings concur with previous evidence from empirical studies on corporate governance, indicating that adoption of the various corporate governance practices by listed agricultural firms plays a part in the improvement of their performance financially. It was concluded that most agricultural firms had not adhered to the rules and guidelines issued by CMA. The valid model explained moderately the variations in performance of the firms and confirmed that corporate governance practices employed by listed agricultural companies in Kenya influence their financial performance.

The study recommends that the Government ought to enforce measures laid down on corporate governance to ensure public organizations are following them.

INTRODUCTION:

CHAPTER ONE

1.1 Background of the Study

The term *governance* is derived from the Latin word *gubernare*, meaning to lead or steer. Thus, this shows that corporate governance includes the function of direction rather than control (Dibra, 2016). Corporate governance is also defined as the control of management for best interests of the company, which include responsibility and accountability to shareholders who elect directors and accountants. Corporate governance can also be defined as accountability to providers of investment (Aggarwal, 2013; Dibra, 2016). Corporate governance is an important feature for the existence of companies and it is a bedrock used by these organisations to realize their goals and objectives. The concept of corporate governance covers such a huge area so that there is not a single definition involving all facets but each explanation reflects a different characteristic of the concept. In short, corporate governance is a set of procedures, customs, guidelines and rules which regulates the running of an organisation towards its objective. Hence, corporate governance aims at managing a firm to make profit and wealth so that each group allied to it is treated in the best way (Padachi, Urdhin, & Ramen, 2016)

This study was supported by four theories namely: stewardship theory, which holds that employees and executives should act more independently so as to maximize shareholders' returns, agency theory which holds that heads of the company are the owner's or shareholders and they employ representatives who are the executives and managers to do the work on their behalf. The organisation owners delegates the

operations of business to the managers or directors, who are shareholder's agents and they are expected to deliver and work towards achieving principals' interest, stakeholder theory Contrasts agency theory as it propose that managers in an organization have a group of connections to serve which included suppliers, members of staff and other business while agency theory talks of managers working for principals only and finally the resource dependency theory where-by it concentrates on provision of resources and the ability of the board of directors to provide avenues of sourcing for finances and availing them to the company. It also extends mandate of board of directors to secure essential resources and providing access to financiers for the company on behalf of the management.

In Kenya, the Capital Markets Act Cap. 485A (2002) specifies that the best procedures for corporate governance in public companies based on approvals and reports from the Organization for Economic Cooperation and Development (OECD), the Commonwealth Association for Corporate Governance and the Private Sector Corporate Governance Trust, Kenya. CMA Act recommends several guidelines. First, there should be separations of Chief Executive Officer and Chairman Position. The board of directors should be made up of 5 and 14 members in number. It also recommends board composition that comprise of at least a third of independent and non-executive directors with different skills, gender and racial stability. Also recommended is the establishment of an audit committee that shall report to the Board comprising of three independent and non-executive directors. It also provides for a formation of an internal audit task, which should be independent from the boards' activities. They audit should be neutral and proficient in their tasks. The board should meet at least quarterly though the meetings can

be increased as per the needs of the company and the meeting dates in a calendar year agreed in advance (CMA Act, 2002).

1.1.1   Corporate Governance Practices

Corporate governance, controls management of the company in the best interests, including accountability to shareholders who chooses directors and auditors and vote on say on pay. Corporate governance can also be defined as accountability to providers of capital. The issues of corporate government have become more visible and the focus by both business leaders and regulators across the globe today. This is because corporate governance had received lack-lustre consideration from corporate organizations globally for an extensive period of time (Gompers and Metrick, 2013).

The abandonment of corporate governance policies have resulted to the recent global high profile corporate disappointments. For example, HIH insurance and One-Tel from Australia were among the failed corporate bodies. Others include the Maxwell Communications Corporation, Bank of Credit, Commerce International in the United Kingdom, WorldCom, and Enron in United States of America and Parmalat from Italy. These corporate disappointments have been alluded to meagre corporate governance practices (Carcello & Neal, 2011).

In Kenya, there have been several corporate failures involving public organizations such as Pan African Paper Mills in Webuye, Kisumu Cotton Mills, Rift Valley Textiles, Kenya Planters Cooperative Union, Miwani sugar factory, and many other privately owned entities. The most recent business failures are financial institutions namely Chase and Imperial banks. These business let-downs raise some essential queries such as

management elegance, audit objectivity, ethics, professionalism, disclosures, personal accountability, and conflict of interest. According to Ikiara (2010), the pure scale of fraud, misappropriation and corruption perceived in some of the unsuccessful government institutions brought into question of the consistency and effectiveness of present day operational and compliance control devices and financial accounting in general. A workshop to develop a Code of Best Practice for corporate governance in Kenya was held at the Kenya College of Communications & Technology in Nairobi in November 1998. It was funded by leading organizations with definite concern in corporate governance namely; Nairobi Stock Exchange, Capital Markets Authority, Institute of Certified Public Accountants and the Kenya Chapter of the Association of Chartered Certified Accountants among others.

Corporate governance has been measured in several ways. For example, Azeez (2015) in a study that analyzed the effect of corporate governance on firm performance in Sri Lanka, India used CEO division, board Size, and proportion of non-executive directors. While Aduda, Chogii and Magutu (2013) in a study all companies quoted at the NSE used board composition, size of the board, proportion of outside and inside directors, and the role of CEO duality. Narwal and Jindal (2015), studied the effect of corporate governance on the productivity of Indian used board size, audit committee members, board meetings, non-executive directors, directors' payments.

1.1.2 Financial Performance

This is a measure a firm's ability to use assets for revenue generation. According to Adams (2003), financial performance is a subjective measure of the accountability of an entity for the results of its policies, operations, and activities quantified for an identified period in financial terms. Financial performance in the public sector is a function of what the public sector entity is held responsible for achieving in profit making within a specified period.

Financial performance is an independent measure of the accountability of an entity for the results of its policies, operations, and activities quantified for an recognized period of time in financial terms. Financial performance in the corporate governance arena has been measured in several ways using accounting. Azeez (2015), analysed the effect of corporate governance on firm performance in Sri Lanka, India used ROE, ROA, and EPS to measure firm performance. On the other hand, Aduda et al. (2013) in a study all companies quoted at the NSE used return on assets and Tobin Q ratio.While Aggarwal (2013) investigating the effect of corporate governance on financial performance of listed companies in India used ROA, ROE, ROCE and PBT.

1.1.3 Corporate Governance and Financial Performance

The questions about why corporate failures occur, re-occurrence prevention in future, and restoring investor confidence are all linked to practices employed by Corporate Governance. There are several merits of effective Corporate Governance. It helps management to ensure appropriate and adequate controls to safeguard assets, checking powers and influence of dominant individuals. It defines the relationship between the company management, the board of directors, shareholders, and other stakeholders. It

aims at ensure that the company is managed in the finest interests of the shareholders and other stakeholders. It inspires accountability and transparency that investors are increasingly looking for in the companies (Padachi, et al., 2016). In sum, well applied corporate governance principles in the business organization may increase profitability and returns, improve its competitiveness, credibility and improve relationships with key shareholders such as investors, business partners, personnel, clients, etc (Todorovic, 2013).

Corporate governance has obtained much consideration throughout the last three decades due to certain economic changes, regional market calamities and large corporate fiascos. A study by Azeez (2015) on a 100 quoted companies in the Colombo Stock Exchange in Sri Lanka for the periods 2010 to 2012 pointed out that there is substantial difference between the firm performance among Corporate Governance practices as board leadership practices, board committees, board meetings and share of non-executive directors. A study by Narwal and Jindal (2015) examined the effect of corporate governance on the profitability in India in the period 2009 to 2014 found a strong positive relationship was observed between director's remuneration and profitability. The study also found audit Committee members had negative associated with the profitability and concluded that board size, board meeting and non-executive directors were insignificantly associated with the profitability.

Galebu (2010) study In Africa on corporate governance effects on the performance of firms which uses both accounting based performance measures and market. Sole data from 103 listed firms drawn from Ghana, South Africa, Nigeria and Kenya covering a

period of five years from 2006 to 2010 and analysis done. Findings indicated that the trend and the extent of the effect of governance were dependent on the performance measure being scrutinised. Explicitly, the findings exhibited that independent and large boards enhance firm value and that conjoining the positions of CEO and board chair had a negative influence on corporate performance.

Muriithi (2004), in a research of 44 Firms listed at the NSE between 1999 and 2003, used a sum of governance variables such as, block ownership, family ownership, foreign ownership, Board size and Board composition. Board composition variable under consideration was the proportion of non-executive directors. It was found that there was no significant relationship, in case of non- executive Board of directors. The study found established that no measure of firm performance had a considerate relationship with board independence.

1.1.4   Agricultural Sector in Kenya

In Kenya, agricultural sector is the backbone of the economy. However, only six out of 54 listed companies in the NSE are agricultural. There are six companies currently listed in the NSE are Williamson Tea company, Sasini limited, Limuru Tea, Kapchoria Tea company, Kazuzi Limited and Eaagad limited after Rea Vipingo limited de-listed in 2014 (NSE, 2016). The Capital Markets Act (Cap 485A) provides procedures on corporate governance practices by public companies in Kenya. The CMA procedures on corporate governance cover such areas as; the rights of shareholders; equitable treatment of shareholders; role of stakeholders; board structures; disclosure and transparency and

board responsibilities. The CMA Code of Best Practice is prescriptive on Board characteristics for companies listed at the NSE (GOK, 2015).

1.2 Research Problem

A number of agricultural companies in Kenya have collapsed. However, enough research has not been done on this sector to enlighten corporate issues affecting it. Previous researchers have been concentrating on Banking sector and other service industries thereby ignoring the agricultural sector yet Kenya's economy depends on agriculture. Notwithstanding tight regulatory structure, corporate governance remains to weaken in Kenya (Aduda et al., 2013). According to Muriithi, (2004), scandals characterize many companies in Kenya and around the world. Directors have served personal interests instead of serving their shareholders. There is a problem in corporate governance as we have witnessed recently in the banking sector where two banks namely Imperial bank and Chase bank have gone under receivership. Others like Mumias Sugar Company, Uchumi supermarket and Kenya Airways are struggling to remain in the market by post poor financial results. Their poor financial performance has been caused directly or indirectly by absence of good corporate governance. The problems of corporate governance in listed agricultural companies have not been exhaustively done.

Empirical studies have revealed a link between corporate governance practices and firm performance in emerging markets; however, few researchers have investigated individual countries in depth. Yasser (2011) studied the impact of corporate governance on performance in Pakistan and revealed that corporate governance structure influences performance. They advised the regulators to be vigilant and to set diverse codes for each type of companies. In his study Aduda et al. (2013) analysed impact of corporate

governance on performance of all listed companies in Kenya but he did not assess the effect of corporate governance on performance individual sectors like agriculture. It is due to these research gaps that the study was undertaken to answer the following question: does corporate governance practices influence financial performance of listed agricultural firms in Kenya.

1.3 Research Objective

The objective of this study was to determine whether corporate governance practices employed by listed agricultural companies in Kenya influence their financial performance.

1.4 Value of the Study

This research will be of importance to listed agricultural companies' management where they can use it to improve on their corporate governance. It will be useful to policy makers who can use it to base their policies on financial improvement and corporate governance. It will extend its worth to the government of Kenya on measures and reforms required to put listed agricultural companies on track again and increase productivity to solve listed agricultural deficit problem.

The study will benefit students, researchers and scholars interested in building on the already prevailing information base about theoretical and empirical work on the corporate governance practices and the subsequent effects on the performance of firms in the listed agricultural industry in Kenya. It will be of significant to academicians who are interested in disseminating knowledge on the subject of corporate governance practices and its effects on the financial performances of firms in the Kenya listed agricultural industry.

CHAPTER TWO:

LITERATURE REVIEW

2.1 Introduction

This chapter highlights the available literature on corporate governance that has been reviewed for the study. Specific areas covered include the main corporate governance theories, empirical literature on the relationship between corporate governance practices and firm performance, empirical evidence on corporate governance practices and financial performance in Kenya and lastly a brief summary of the literature reviewed.

2.2 Theoretical Review

Several theories have been advanced towards justification of corporate governance practices. For the purpose of this research, four theories being the stewardship theory, agency theory, stakeholder's theory and resource dependency theory shall be advanced.

2.2.1 Stewardship Theory

Stewardship theory has its roots from psychology and sociology. According to Donaldson and Davis (1991), a steward maximizes and protects shareholders wealth through firm performance, because by doing so, the steward's utility functions are maximized. In this perception, stewards are company managers and executives working for the shareholders, protects and make profits for the shareholders. Stewardship theory holds the doctrine of executives or employees to act more autonomously so that the shareholders' returns are maximized. Indeed, this can minimize the costs aimed at controlling and monitoring behaviours. As stewards, they are essentially presumed to be trustworthy individuals and

therefore good stewards of the resources entrusted to them, which makes monitoring redundant (Donaldson & Davis, 1991).

Donaldson and Davis (1991) argued that in order to protect their reputations as decision makers in organizations, executives and directors are inclined to operate the firm to maximize financial performance as well as shareholders' profits. In this sense, it is believed that the firm's performance can directly impact perceptions of their individual performance. Moreover, stewardship theory suggests unifying the role of the CEO and the chairperson so as to reduce agency costs and to have greater role as stewards in the organization. It was evident that there would be better safeguarding of the interest of the shareholders.

2.2.2 Agency Theory

Agency theory having its origins in economic theory was exposited by Alchian and Demsetz (1972) and further developed by Jensen and Meckling (1976). Agency theory is defined as the relationship between the principals, such as shareholders and agents such as the company executives and managers. In this theory, shareholders who are the owner's or principals of the company, hire agents to perform the work. Principals delegate the running of business to the directors or managers, who are shareholder's agents (Donaldson and Davis, 1991).

All parts of participants dream uniform standards of corporate governance. This is the key driver for corporate governance convergence. The Organisation for Economic Cooperation and Development (OECD) Principles of Corporate Governance is the first conceptual framework for policy makers, companies, and others around the world

(OECD, 1999). However, all countries, emerging or emerged, have the problem of principal-agent costs, and each has a distinctive set of rules to deal with the problems caused by agency costs. Corporate governance models differ in each country's business framework as companies in different countries operate under a different business culture and different legal and economic systems.

2.2.3 Stakeholders Theory

Stakeholder theory was implanted in the management discipline in 1970s and gradually developed by Freeman (1999) incorporating corporate accountability to a broad range of stakeholders. Donaldson and Preston (1995) argued that stakeholder theory was derived from a combination of the sociological and organizational disciplines. Indeed, stakeholder theory is less of a formal unified theory and more of a broad research tradition, incorporating philosophy, political theory, ethics, law, economics, and organizational science. According to the theory, a stakeholder is any group or individual who can affect or is affected by the achievement of the organizations objectives. Unlike agency theory where by managers work and serve the stakeholders, stakeholder theorists suggest that managers in organizations have a network of relationships to serve, this include the suppliers, employees and business partners (Freeman, 1984; Freeman, 1999).

2.2.4 Resource Dependence Theory

Whereas the stakeholder theory focuses on relationships with many groups for individual benefits, resource dependence theory focuses on the role of Board of Directors in availing ways leading to access resources needed by the firm. Hillman, Canella and Paetzold (2000) contend that resource dependence theory focuses on the role that directors play in providing or securing essential resources to an organization through their linkages to the

external environment. Indeed, Johnson, Daily and Ellstrand (1996) concludes that resource dependency theorists provide emphasis on the appointment of representatives of independent organizations as a means for gaining access in resources critical to firm success. In sum, boards of directors have the power to make and ratify all-important decisions including decisions about investment policy, management compensation policy, and board governance itself (Bhagat & Bolton, 2008).

2.3 Measurement of Financial Performance

According to Williamson (1996), financial performance is a subjective measure of how well a firm can use assets from its primary mode of business and generate revenues. This term is also used as a general measure of a firm's overall financial health over a given period, and can be used to compare similar firms across the same industry or to compare industries or sectors in accretion. Financial performance can be measured using five variables that include, namely profitability ratio, solvency ratio, liquidity ratio, financial efficiency ratio and finally the repayment capacity of an entity for given period For example Aggarwal (2013) investigated the effect of corporate governance on financial performance in India used ROA, ROE, ROCE and PBT. Whilst Aduda et al., (2013) measured performance using ROE and Tobin Q ratio. Yet Azeez (2015) when analysing the effect of corporate governance on firm performance in Sri Lanka, India. Measure firm performance using ROE, ROA, and EPS.

2.4 Determinants of Corporate Governance

2.4.1   Size of the Board

Azeez (2015) show board size was negatively related with firm performance. This implies that small boards are related with higher firm performance possibly through close

supervision management. This expression is inconsistent with the inference of Malik, Wan, Ahmad, Naseem and Rehman (2014) that provides empirical evidence that board size positively affect firm performance. Narwal and Jindal (2015) in a study in India found board sizes were insignificantly associated with the profitability.

2.4.2 Board Audit Committees

The audit committee's role has come under inquiry in recent years. In response, both minimum prerequisite requirements for audit committee membership and required public disclosure over audit committee processes have increased (Carcello & Neal, 2011). High profile corporate frauds have heightened the requirement for an effective audit committee in companies. Frequent meetings, independence and numbers of members of audit committee can ensure credibility and quality of financial reports (Aggarwal, 2013). A study by Malik et al. (2014) found positive correlation between audit committee and firm performance. They concluded that a strong audit committee would assist the firms to achieve better performance. Narwal and Jindal (2015) in a study in India found audit committee members were negatively associated with the profitability

2.4.3 Board Structure

Non-executive directors on boards are intended to monitor, supervise and control the activities of executive directors. The presence of non-executive directors should reduce their opportunistic behaviour by acting as the checks and balances thereby enhancing boards' effectiveness (Jensen & Meckling, 1976). Further, non-executive directors may be viewed as "decision experts" (Fame & Jensen, 1983). A study by Tusiime, Nkundabanyanga and Nkote (2011) show variance in performance could be explained by

ownership structure and board structure. The study concluded that it is necessary to reduce government ownership so as to achieve better performance.

2.4.4   Board Independence

Independence of Board is widely believed to play a significant role in monitoring and advising the company's management. They are also required to safeguard overall organizational and stakeholders interest (Aggarwal, 2013). In most cases, independent directors are not intimidated by the CEO. Therefore, they are also able to reduce managerial consumption of perquisites and act as a positive influence over directors' deliberations and decisions. The presence of independent directors on boards provides additional decision window in the company (Fama & Jensen, 1983). This is congruent with the resource dependence theory, which proposes that independent directors act as middleman between companies and the external environment due to their expertise, prestige and contacts (Yasser, 2011).

2.5 Conceptual Framework

The independent variables in the conceptual framework are as explained below -

Independent variables   **Dependent variable**
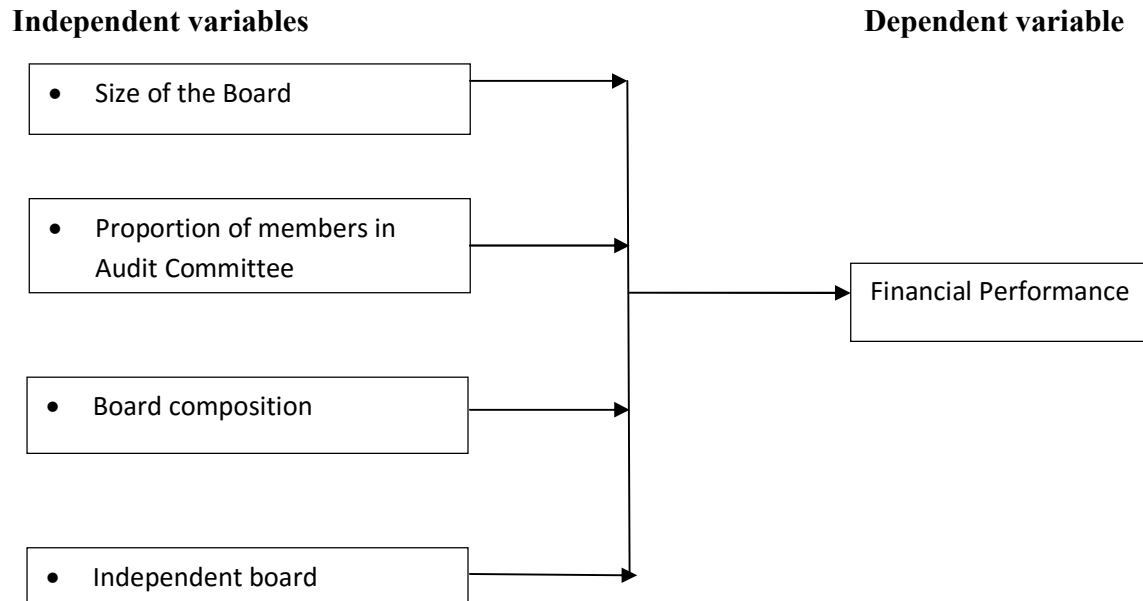
Source (Researcher, 2017)

Figure 2.1: Conceptual framework

2.6 Empirical Review

Yasser (2011) examined the impact of corporate governance on family and nonfamily controlled companies' performance in Pakistan. The sample size of this study is 792 companies listed on Karachi Stock Exchange from 2003 to 2008. The findings revealed that corporate governance structure influences the family and non-family controlled companies' performance. However all corporate governance mechanisms were not significant. The significant variables differ between family and non-family controlled companies. Thus, regulators need to be vigilant that family and non-family controlled companies practice differently and to set different codes for each type of companies.

A study byTusiime, Nkundabanyanga and Nkote (2011) examined ownership structure, board structure and their relationship performance in public sector companies in Uganda. They study used 85 public sector entities in Uganda. The findings shoe that, CEO duality is not key as far as the performance was concerned. Findings show variance in performance could be explained by ownership structure and board structure. The study concluded that it is necessary to reduce government ownership so as to achieve better performance.

Aggarwal (2013) investigated the effect of corporate governance on financial performance in India using 20 listed companies. Various tests such as regression, correlation, t-test and F-test were performed using secondary data for of two years- 2010-11 and 2011-12. The dependent variable were ROA, ROE, ROCE and PBT. The independent variables wee employees-related, community-related and environmental dimensions. The study also controlled for size of firm. The study found that corporate governance had positive and significant impact on financial performance.

A study by Malik et al., (2014) examined the relationship between board size and firm performance. This relationship was tested using the Pareto Approach for Pakistani banking. A sample of 14 listed banks of Pakistan for 2008-2012 was used. Different models were applied to test the effect of corporate governance practices on bank performance. The results were contradictory with the extant studies on corporate governance variables and firm performance. The foremost finding was that there was significant positive relationship between board size and bank performance. It was concluded that a large board size could enhance the bank performance in Pakistani.

Aduda et al. (2013) assessed the significance of the board composition, size of the board, proportion of outside directors, proportion of inside directors, and the role of CEO duality on firm performance. All companies quoted at the NSE were analysed for period of four years from 2004 to 2007. The study measured firm performance by the Return on Assets and Tobin Q ratio. This study found that the overall regression models for firm performance for both the Return on Assets and Tobin Q ratio are significant. This implies that the corporate governance variables above were important for firm performance.

Azeez (2015) analyzed the effect of corporate governance on firm performance in Sri Lanka, India. CEO duality, board Size, and proportion of non-executive directors were used as corporate governance dimensions. ROE, ROA, and EPS were the measures of firm performance used. Data was obtained from the financial reports of 100 quoted companies in the Colombo Stock Exchange for the years 2010-2012. OLS regression findings show that board size was negatively related with firm performance. This implies that small boards are related with higher firm performance, possibly through close supervision management. Moreover, the results show that the separation of the two positions of CEO and chairman has a significant positive effect on the firm performance. However, presences of non-executive directors was not related with firm performance.

A study by Narwal and Jindal (2015) examined the effect of corporate governance on the profitability of Indian textile sectors. The data was collected from annual reports of textiles companies for five year from 2009-2010 to 2013-2014. The profitability was the dependent variable. Board size, audit committee members, board meetings, non-executive directors, directors remunerations were independent variables. Data analysis by

was correlation and OLS regression model. A strong positive relationship was observed between director's remuneration and profitability. The Audit Committee members had negative associated with the profitability. The study concluded that board size, board meeting and non executive directors were insignificantly associated with the profitability.

None of these studies had considered listed agricultural companies in Kenya using ROA, ROE and debt equity ratio. To fill the existing gaps, this study sought to establish the influence of corporate governance practices on financial performance in listed agricultural firms in Kenya.

2.7 Summary of Literature Review and Research Gap

Understanding the need for good corporate governance is the first step on the path to successful implementation of corporate governance mechanisms. There is need to understand the issues that each organization has and how good corporate governance mechanisms help to achieve the maximum benefit. The effects of corporate governance on the firms' performance have been subject to various empirical studies in the literature review. Different studies highlighted have yielded mixed results. Nevertheless, the studies are characterized by a lack of normalization whereby they differ in terms of choice of governance mechanisms, country focus, the choice of the statistical methodology being applied and data sources.

CHAPTER THREE: RESEARCH METHODOLOGY

3.1 Introduction

This chapter discusses how research will be conducted. It analyses the research design, population of the study, sample size, data collection and data analysis. Research is defined as the process of arriving at a dependable solution to a problem through planned methods and interpretation of data.

3.2 Research Design

Descriptive correlation research design was adopted as it enabled the study to assess the existence of any influence of corporate governance practices on financial performance in listed agricultural firms in Kenya. The design involves a set of methods and procedures that describes the intended variables and how they relate to each other (Mugenda and Mugenda, 2003). Descriptive research was used to obtain information concerning the current status of a phenomenon to describe what existed with respect to variables in a situation.

3.3 Population of the Study

The population of this study consisted of seven agricultural firms listed in the Nairobi Securities Exchange in the period 2012 to 2016.

3.4 Data Collection

The researcher used secondary sources. Secondary sources of data were taken from published audited annual reports and financial statements for the selected firms in the listed agricultural industry. Financial data included statements of financial position, comprehensive income as well as cash flow statements relating to the period under study.

Secondary data was collected for the period of five years between 2012 and 2016 for except Rea vipingo whose data was for 2012 to 2014. This yielded 33 data points.

3.5 Data Analysis

Data was analysed using Statistical Package for Social Sciences (SPSS) version 21. Descriptive statistics including mean, standard deviations, minimum and maximum. Tables were used to present the data to enable ease of understanding and analysis. Correlation and multiple regression analysis were used to find out whether the independent variables predicted the given dependent variable.

3.5.1   The Regression Model

A multiple regression model of financial performance versus corporate governance practices was applied to test the relationship between the variables. The study used ROE, ROA and debt equity ratio for 5 years for each company as the measure of financial performance. Several studies (Aduda et al., 2013; Azeez, 2015) have used more than one measure of financial performance. For example, Aduda et al. (2013) used ROA and Tobin Q ratio while Azeez (2015) used three measures namely ROE, ROA, and EPS. The model treated financial performance as the dependent variable while the independent variables were the board size, board composition, presence of audit committees and independence of board committees. Size of the Board was measured by the number of the board members sitting in a full board meeting, board composition the ratio of executive to non-executive directors, independence of board committees by number of independent directors in the committee and proportion of directors in audit committees to the entire board.

Equation 4.1 presents the linear model applied;

$$Y_i = \beta_o + \beta_1 BS + \beta_2 BC + \beta_3 IB + \beta_4 AC + e \dots\dots\dots\dots\dots\dots\dots\dots\dots\text{Equation 4.1}$$

Where: Y_i = performance (Y_1=ROA; Y_2= ROE; Y_3=Debt Equity Ratio)

β_o = Constant of the model

$\beta_1 - \beta_4$ =Regression coefficients

BS = Board size

BC = proportion of executive and non-executive board members

IB = proportion of independence of board members

AC = proportion of directors in the audit committees

e = error term

CHAPTER FOUR

DATA ANALYSIS, RESULTS AND DISCUSSIONS

4.1 Introduction

This chapter presents the interpretation and data analysis on the study to determine corporate governance practices and their influence on the financial performance of agricultural firms listed in the NSE in Kenya. The study was directed to all the seven firms, which traded during the period 2012 to 2016.

4.2 Descriptive Analysis of the Study Variables

The data was summarized and descriptive statistics of mean and standard deviation calculated for the respective variables. The resultant mean values of the independent variables were then regressed against the dependent variable. Data analysis was done through Statistical Package for Social Sciences (SPSS) Version 21. Descriptive statistics were done using percentages, means and standard deviations The seven agricultural companies are Williamson Tea company (WT), Sasini limited (SL), Limuru Tea (LT), Rea Vipigo (RV), Kapchoria Tea company (KT), Kakuzi Limited (KL) and Eaagad limited (EL)

Table 4. 1: ROA in Percent

	WT	SL	LT	RV	KT	KL	EL	Mean
Mean	6.96	4.73	15.59	10.64	2.69	10.99	-4.67	7.15
S. D	6.60	8.00	61.30	3.78	5.37	5.07	7.14	25.80
Min.	-2.65	-0.75	-97.93	6.69	-1.11	4.44	-11.82	-97.93
Max.	11.79	22.46	83.37	15.67	6.48	16.88	3.67	83.33

Source: Researcher, 2017

Table 4.1 shows that the mean for ROA was 7.15%. Sasini limited, Eaagad limited and Kapchorua Tea Company had below the average ROA. While Limuru tea company had the highest ROA and also the highest standard deviation.

Table 4. 2: ROE in Percent

	WT	SL	LT	RV	KT	KL	EL	Mean
Mean	9.79	2.19	24.09	14.77	7.25	15.39	-5.78	10.09
Std. Dev.	9.22	2.43	152.33	4.42	8.05	7.43	8.7	55.78
Minimum	-3.45	-1.04	-216.34	10.42	-1.54	5.68	-14.64	-216.34
Maximum	17.27	5.79	206.52	20.92	14.25	23.37	4.37	206.52

Source: Researcher, 2017

Table 4.2 indicates that the mean for ROE was 10.09%. Sasini limited, Eaagad limited and Kapchorua Tea Company had ROE below the average. While Limuru tea company had the highest ROE and also the highest variability.

Table 4. 3: Debt equity ratio

In this section, Pearson correlation was used to show the direction of influence and magnitude of the relationship of the independent variable to the dependent variable.

	WT	SL	LT	RV	KT	KL	EL	Mean
Mean	0.37	0.27	0.72	0.41	0.39	0.39	0.25	0.40
Std. Dev.	0.07	0.15	0.58	0.12	0.01	0.09	0.12	0.27
Minimum	0.30	0.09	0.28	0.29	0.39	0.27	0.15	0.09
Maximum	0.46	0.42	1.48	0.56	0.40	0.49	0.46	1.48

Source: Researcher, 2017

Table 4.3 indicates that the mean for debt equity ratio was 40%. Limuru Tea Company and Rea vipingo had debt equity ratio above the average. While Eaagad limited had the lowest debt equity ratio whereas Kapchorua Tea Company had lowest variability.

Table 4.4: Descriptive statistics on profit after Tax in Millions

	WT	SL	LT	RV	KT	KL	EL	Mean
Mean	555.00	1183.14	33.80	288.75	51.50	382.00	-21.75	259.41
Std. Dev.	524.22	2188.12	224.92	132.67	103.94	193.26	35.472	328.92
Minimum	-227.00	-67.00	-331.00	153.00	-22.00	160.00	-59.00	-331.00
Maximum	855.00	6067.00	285.00	444.00	125.00	644.00	21.00	974.00

Source: Researcher, 2017

Table 4.4 show that the mean profit after tax was 259.41 million. Limuru tea company, Kapchorua Tea and Eaagad limited had profit after tax below the average. While Eaagad limited had the lowest profit after tax. Sasini limited had the highest variability.

Table 4. 5: Descriptive statistics on total assets in Millions

	WT	SL	LT	RV	KT	KL	EL	Mean
Mean	8,252	18,595	269	2,642	1,955	3,428	532	5,531
Std. Dev	823	10,258	88	458	38	354	75	7,473
Minimum	7,243	8,922	158	2,248	1,928	2,853	445	158
Maximum	9,184	30,851	342	3,202	1,982	3,816	615	30,851

Source: Researcher, 2017

Findings in Table 4.5 depict that the mean total assets was 5.531 billion. Williamson Tea Company and Sasini limited had total assets above the average. While Limuru Tea company had the lowest total assets. Whereas Sasini limited had highest variability.

Table 4. 6: Descriptive statistics on Total liabilities in Millions

	WT	SL	LT	RV	KT	KL	EL	Mean
Mean	2,188	2,669	109	742	551	938	271	1,126
Std. Dev.	157	154	79	51	5	139	411	987
Minimum	1,975	2,485	38	711	547	770	80	38
Maximum	2,315	2,857	204	819	555	1,111	1,007	2,857

Source: Researcher, 2017

Findings in Table 4.6 depict that the mean total liabilities was 1.126 billion. Sasini limited had total liabilities above the average. Eaagad limited had the highest variability. While Limuru Tea company had the lowest total liabilities

Table 4. 7: Descriptive statistics on Board Size

	WT	SL	LT	RV	KT	KL	EL	Mean
Mean	7	9.14	3.00	5.00	7.50	5.67	3.00	5.75
Std. Dev.	0	1.46	0.00	0.00	0.71	2.58	0.00	2.44
Minimum	7	7	3	5	7	2	3	2.00
Maximum	7	11	3	5	8	8	3	10.00

Source: Researcher, 2017

The study sought to determine the number of the board of director members. Table 4.7 indicates that the mean board members were 5.75. Williamson Tea, Sasini limited and Kapchoria Tea had board sizes above the average. While Limuru Tea Company and Eaagad limited had the smallest boards of three and they had violated CMA Act minimum threshold of five directors. Whereas Sasini limited had highest variability.

Table 4. 8: Descriptive statistics on the Board Structure or Composition

	WT	SL	LT	RV	KT	KL	EL	Mean
Mean	40.00	14.08	200.00	25.00	15.48	48.89	200.00	78.21
Std. Dev.	0.00	3.37	0.00	0.00	1.68	10.68	0.00	78.53
Minimum	40.00	11.11	200.00	25.00	14.29	33.33	200.00	11.11
Maximum	40.00	20.00	200.00	25.00	16.67	60.00	200.00	200.00

Source: Researcher, 2017

The study sought to determine the percentage of executive to non-executive director. The CMA Act (2002) recommends that at least a third of the directors should be non-

executive. Table 4.8 indicates that the mean board structure was 78.21%. Generally, this is poor board composition. Limuru Tea company and Eaagad limited had board structures where the executive director were double those who non-executive. Whereas Kakuzi limited and Williamson Tea had, 48.89% and 40% board composition composition respectively. Therefore, only Sasini limited, Rea vipingo and Kapchoria Tea had obeyed the CMA Act.

Table 4. 9: Descriptive statistics on Audit Committees of the Board

	WT	SL	LT	RV	KT	KL	EL	Mean
Mean	2	3.33	0.00	3.00	2.00	4.00	0.00	2.19
Std. Dev.	0	.516	0.00	0.000	0.000	0.00	0.00	1.55
Minimum	2	3	0	3	2	4	0	0
Maximum	2	4	0	3	2	4	0	4

Source: Researcher, 2017

The study sought to determine the number of directors in the audit committee. The CMA Act (2002) recommends at least three independent and non-executive directors who reports directly to the full board. Table 4.9 indicates that the mean audit committee size was 2.19. Limuru Tea Company and Eaagad limited did not board have audit committees. Williamson Tea and Kapchoria Tea Company had two directors each. Therefore, Limuru Tea Company, Eaagad limited, Kapchoria Tea and Williamson Tea Company had violated the CMA Act threshold of three members.

Table 4.10: Proportion of independent directors

	WT	SL	LT	RV	KT	KL	EL	Mean
Mean	42.86	24.67	0.00	40.00	0.00	60.62	0.00	25.62
Std. Dev.	0.00	29.69	0.00	0.00	0.00	31.01	0.00	27.07
Minimum	42.86	10.00	0.00	40.00	0.00	33.33	0.00	0.00
Maximum	42.86	90.91	0.00	40.00	0.00	100.00	0.00	100.00

Source: Researcher, 2017

The study sought to determine the proportion of independent directors in the board. The CMA Act (2002) recommends a majority. Table 4.10 indicates that the mean proportion of independent directors was 25.62%. Limuru Tea Company, Williamson Tea Company and Eaagad limited did not have independent directors in board. Therefore, only Kakuzi limited had achieved the benchmark set by the CMA Act.

4.3 Correlation Analysis of the Study Variables

Table 4. 11: Correlation matrix for ROA

	ROA	BS	IB	AC	BC
ROA	1				
BS	-.186	1			
IB	-.166	.523[**]	1		
AC	-.172	-.025	.596[**]	1	
BC	.282	-.706[**]	-.543[**]	-.503[**]	1

**p<.001

Source: Researcher, 2017

Results in Table 4.11 show there was weak negative correlation between corporate governance practices and ROA except with Board composition. The highest correlation coefficient is 0.282 indicates weak positive correlation between corporate governance practices and ROA. The highest correlation coefficient is 0.706 between board composition and board size. Since none of these correlation coefficients between the independent variables is greater than 0.8, there is no multicollinearity.

Table 4. 12: Correlation matrix for ROE

	ROE	BS	IB	AC	BC
ROE	1				
BS	-.185	1			
IB	-.165	.523[**]	1		
AC	-.172	-.025	.596[**]	1	
BC	.282	-.706[**]	-.543[**]	-.503[**]	1

**p<.001, *p<.05

Source: Researcher, 2017

Results in Table 4.12 show there was weak negative correlation between corporate governance practices and ROE except with Board composition. The highest correlation coefficient is 0.282 indicates weak positive correlation between corporate governance practices and ROE. The highest correlation coefficient is 0.706 between board composition and board size. Since none of these correlation coefficients between the independent variables is greater than 0.8, there is no multicollinearity.

Reviewing results in Table 4.11 and 4.12. corporate gorvernace practices have negative correlation with ROA and ROE. This a similar to a study by Azeez (2015) which analysed the effect of corporate governance on firm performance in Sri Lanka The study found that board size is negatively related with firm performance. It concluded that small boards are related with higher firm performance, possibly through close supervision management. Whilst a study by Narwal and Jindal (2015) examining the effect of

corporate governance on the profitability of companies in India found audit committee members had negative associated with the profitability.

Table 4. 13: Correlation matrix for Debt equity ratio

	DE	BS	IB	AC	BC
DE	1				
BS	.347*	1			
IB	.472**	.523**	1		
AC	-.070	-.025	.596**	1	
BC	-.119	-.706**	-.543**	-.503**	1

$**p < .001$, $*p < .05$

Source: Researcher, 2017

Results in Table 4.14 show there was weak positive correlation between board size and independent board and debt equity ratio while it was negative with audit committee and board composition. The highest correlation coefficient is 0.472 indicates moderate positive correlation between independent board practice and debt equity ratio. The highest correlation coefficient is 0.706 between board composition and board size. Since none of these correlation coefficients between the independent variables is greater than 0.8, there is no multicollinearity.

4.4 Regression Analysis

Under this research, multiple regression analysis was conducted to test the influence among predictor variables. The study used the mean increase in ROA, ROE and debt equity ratio over 5 years' period as the dependent variable and corporate governance

practices as independent variables. The research used statistical package for social sciences (SPSS) version 21 to code, compute and enter the measurements of the multiple regressions. The independent variables in the regression model were board size, board composition, independence of board committees and size of audit committees

Table 4. 14: Regression Model Summary

	ROE	ROA	Debt equity ratio
R	.284	.284	.659
R^2	.081	.081	.435
Adjusted R	-.51	-.051	.357
Standard error	36.85998	1486.76315	.34173

Source: Researcher, 2017

Results in Table 4.13 show the coefficients of determination (R^2) values are sufficiently low (i.e. less than .50) for ROE and ROA implying low predict power while that for Debt equity ratio is high. The R^2 indicates the variation in ROE and ROA due to changes in independent variables. Table 4.13 show that there was a 28.4 % variation in ROE and ROA performance were due to changes in Board size, Board composition, independence of board and audit committees while 65.9% variation in debt equity ratio were due to changes in Board size, Board composition, independence of board and audit committees.

Table 4. 15: ANOVA –ROA

Model		Sum of Squares	df	Mean Square	F	Sig.
	Regression	3332.998	4	833.250	.613	.657[b]
	Residual	38042.430	28	1358.658		
1	Total	41375.428	32			

a. Dependent Variable: ROE

b. Predictors: (Constant), AC, BS, IB, BC

Source: Researcher, 2017

Results in Table 4.15 show F value is not significant compared to P value of .657. Thus, the model fit not valid and therefore could not predict ROA significantly.

Table 4. 16: ANOVA –ROE

Model		Sum of Squares	df	Mean Square	F	Sig.
	Regression	5443239.306	4	1360809.826	.616	.655[b]
1	Residual	61893010.516	28	2210464.661		
	Total	67336249.822	32			

a. Dependent Variable: ROA

b. Predictors: (Constant), AC, BS, IB, BC

Source: Researcher, 2017

Results in Table 4.15 show the significance of F values is more than .05(p=.655). Thus, the model fit not valid and therefore could not predict ROA significantly.

Table 4. 17: ANOVA –Debt Equity Ratio

Model		Sum of Squares	df	Mean Square	F	Sig.
	Regression	41658.019	4	10414.505	5.435	.002[b]
1	Residual	53651.257	28	1916.116		
	Total	95309.276	32			

a. Dependent Variable: DE

b. Predictors: (Constant), AC, BS, IB, BC

Source: Researcher, 2017

Results in Table 4.16 show the significance of F values is less than .05 (p=.002). Thus, the model fit is good and therefore could predict debt equity ratio with 0.2% variation significantly. From the Table 4.16 the p- value was 0.02, which shows that the model was statistically significant.

Table 4.18: Regression Coefficients

	ROE		ROA		Debt equity ratio	
	Beta	T-value	Beta	T-value	Beta	T values
BS	0.007	0.016	0.007	0.015	-.356	-0.975
IB	-0.007	-0.019	-0.008	-0.022	1.010	3.745**
BC	0.267	0.606	0.268	0.607	-.219	-0.656
AC	-0.032	-0.076	-0.031	-0.072	-.791	-2.437*

**p<001,*p<.05

Source: Researcher, 2017

Results in Table 4.17 show the All beta coefficients for ROE and ROA are insignificant (p>.05). Thus, corporate governance practices have insignificant effect on ROE and

ROA. The p-values for independence of board and size of audit committee are less than .05. Thus, corporate governance practices have significant effect on debt equity ratio. From the Table 4.17 the regression equation was; Debt equity ratio = 3.745IB - 2.437AC where; IB = proportion of Independent board to entire board and AC = proportion of audit committee to entire board.

This is similar to a study by Yasser (2011) examining the impact of corporate governance on performance in Pakistan that found all corporate governance mechanisms was not significant. Yet a study by Azeez (2015) analyzing the effect of corporate governance on firm performance in Sri Lanka fund presences of non-executive directors was not related with firm performance. Whilst a study by Narwal and Jindal (2015) examining the effect of corporate governance on the profitability of companies in India concluded that board size, board meeting and non-executive directors were insignificantly associated with the profitability.

However, a study by Aduda et al., (2013) using 5 variables for the all listed companies in NSE found that the overall regression models for firm performance for both the Return on Assets and Tobin Q ratio are significant. The study concluded that the corporate governance practices were important for firm performance. Yet a study by Malik et al., (2014) which examined the relationship between board size and firm performance concluded that a large board size could enhance the bank performance in Pakistani.

CHAPTER FIVE

SUMMARY, CONCLUSIONS AND RECOMMENDATIONS

5.1 Introduction

From the data collected and analysis, the following discussions, conclusions and recommendations were made. The responses were based on the objectives of the study. The researcher projected to investigate the influence of corporate governance practices on financial performance of listed agricultural firms in Kenya.

5.2 Summary of Findings

The research found out that compliance to best practice recommendations by the government and other professional associations in Kenya is quite impressive as is attested to by the statistics analyzed. Out of the seven firms, finding show the firms had above e mean score for ROA and ROE. The risk in debt is minimal because the mean debt equity ratio was 40% with only two firm having debt equity ratio of above 40%. Only two firms did not report loss in the period of study and profits after tax have wide deviations for all companies. Only companies have total assets of less one billions Kenya shillings whereas five companies owe less than one billions Kenya shillings.

The largest board has 11 directors while the smallest has three. Two companies had violated the CMA Act minimum threshold of five directors. A board composition of at least a third of executive and non-executive directors of diverse skills and expertise is recommended. Results shows board composition is poor and two companies had obeyed the CMA Act with respect to board composition. Three companies did not have independent directors in board and only one had achieved the benchmark set by the CMA

Act. The audit committee should have diversity in expertise and professions so as to indicate a wealth of knowledge and skills which can result into good decision making thus good financial performance. The CMA Act (2002) recommends at least three independent and non-executive directors who reports directly to the full board. Two companies did not board have audit committees while another two companies had two. This means four companies had violated the CMA Act threshold of three directors in the audit committee.

Board size, independence of board and audit committee correlated negatively with both, ROA and ROE while board composition related positively. Board size, independence of board correlated positively with debt equity ratio while audit committee and board composition related negatively. The linear regression model for ROA and ROE were invalid while that for debt equity ratio was valid. This means corporate governance practices can only predict debt equity ratio significantly where the the regression's correlation coefficient was strong. While the coefficient for determination is moderate. The debt equity ratio model also had the least standard error. Very important, only independence of board and audit committee in the debt equity ratio model significant affects performance.

5.3 Conclusions of the Study

Most agricultural firm have not adhered to the rules and guidelines issued by CMA. Corporate governance practices lead to reduced debt related risks. The valid model only moderately explains the variations in performance of the firms due to changes in Board size, Board composition, and independence of board committees and proportion of audit committee. This answers to the objective of the study and confirms that corporate

governance practices employed by listed agricultural companies in Kenya influence their financial performance.

5.4 Recommendations

The study recommends among other things that the government ought to enforce the measures it has laid down on corporate governance to ensure public organizations are following them. The concerned ministries should also be keen in the supervisory role through the relevant committees to ensure that all regulations are enforced as required. Number of independent directors in board committees should also be maintained at above three as only about half of the corporations were in compliance. More professional experts should be included in the boards to bring in diverse experiences and different ways of doing things. This would bring favourable outlook to the firms which can be of paramount importance when seeking international financial grants, debts and business partnerships.

5.5 Limitations of the Study

The limitations of the study included restricted access to information especially the audited annual reports in the website of the companies. Some published reports were incomplete and extra effort was required to look for information from other forums other than official websites. Other sites are protected and one has to subscribe so as to access information.

5.6 Suggestions for Further Research

The study purports that good performance of organizations is influenced in a way by corporate governance practices. Nevertheless, the study does not responsively rule out the

fact that some other variables in the industry atmosphere could be critical for public organizations performance. Hence, future research could usefully focus on corporate governance practices in other organizations; for example in the education sector, mining sector, manufacturing sector, communication sector among others.

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