THE EFFECT OF CORPORATE GOVERNANCE ON THE
FINANCIAL PERFORMANCE OF SACCOS REGULATED BY
SASRA

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The research project is my original work and has not been submitted for any award in the University

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DEDICATION

I dedicate this study to my wife and my son for the support, understanding and encouragement that they have provided during all the years of my studies and as I prepared and worked on this project. I love you all.
ABSTRACT

The main objective of this study was to investigate the effects of Corporate Governance on the financial performance of saccos regulated by SASRA. Specifically, this study examined board size – number of board members within a financial year, diversity (Gender) - number of women on the board, the compensation of the board - average compensation of all directors on the board, and the working experience of the board and how they affect the financial performance of saccos regulated by SASRA. Saccos financial performance was measured using Return on Assets (ROA). This study adopted a descriptive research design. The population of the study was all deposit taking saccos regulated by SASRA as at 2013. Secondary data was collected using documentary information from SASRA website, and saccos supervisory reports for the period 2009 to 2013.

Descriptive statistics was used. Data was analyzed using a multivariate regression model. The study found board diversity, compensation and size affects the financial performance of deposit taking saccos positively. The board size - that is the number of serving board members in a given financial year was found to negatively affect the financial performance of saccos, the board experience as measured by number of years served in the board was also found to negatively affect the financial performance of saccos and firms age - that is the number of years the sacco has been operating since establishment, were found to negatively affect the financial performance of saccos.

The study found a negative relationship between the number of board members and saccos’ financial performance. It is therefore important to ensure that there should not be too many members on the board because a larger board’s size will contribute negatively to firm’s performance. Increase in number of women on board leads to an increase in saccos’ financial performance. The shareholders should appoint female board members, as they were found to contribute positively sacco’s performance. The study also found out that as board members compensation increased the firms’ financial performance
improved significantly; hence good compensation of the board members contributes positively to the firms’ financial performance.
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LIST OF ABBREVIATIONS

1. ANOVA: Analysis of Variance
2. CEO: Chief Executive Officer
3. CMA: Capital Markets authority
4. EPS: Earnings per share
5. FOSA: Front Office Saving Activities
6. GDP: Gross Domestic Product
7. ISS: Institutional Shareholder Services
8. MBA: Master of Business Administration
9. MFIs: Micro Finance Institutions
10. NSE: Nairobi securities exchange
11. OECD: Organisation of Economic Co-operation and Development
12. ROA: Return on Assets
13. ROE: Return on Equity
14. SASRA: Sacco Society Regulatory Authority
15. SPSS: Statistical Package For Social Science
16. UON: University of Nairobi.
CHAPTER ONE: INTRODUCTION

1.1 Background of the Study

Over the last three decades, corporate governance has become an interesting topic of discussion worldwide and the history is now well documented. According to Choge (2013), the African continent has not been left behind and corporate governance has assumed highest propositions. This is probably due to the great push from the developing countries to the African countries to embrace good governance in order to attract foreign investors and to improve shareholders value.

According to Gomez (2005), there has been significant transformation in corporate governance structures, leading to increased scholarly interest in the role of board of directors in driving corporate performance. This has resulted from many high profile corporate failures, coupled with generally low corporate profits across the globe, which has put the credibility of the existing corporate governance structures into question. Investors have therefore regarded corporate governance as an important criterion in their investment decisions. The unexpected financial distress of large public companies in recent years, for example Enron and WorldCom in 2002, has made the investors more concerned about the corporate governance and firms’ performance.

The Organisation of Economic Co-operation and Development (OECD), (2004) principles of corporate governance acknowledge that an effective corporate governance system can lower the cost of capital and encourage firms to use resources more efficiently, thereby promoting growth. These factors implicitly and explicitly support the
belief that better corporate governance will result in higher firm value and more profitable firm performance.

There are corporate governance issues that arise due to the separation of ownership and management. Principal-agent theory is the starting point of most discussions of corporate governance (Shleifer & Vishny, 1997). Agency problems can affect firm value and performance via expected cash flows for investors, and the cost of capital. First, agency problems make investors pessimistic about future cash flows being diverted. Good governance increases investor trust and willingness to pay more and renders managers’ actions costly and expropriation less likely. Due to agency problems corporate governance is expected to serve as a tool to give confidence to investors that they will receive a return on the funds they have invested. Corporate governance relates to how investors believe that managers will not steal or embezzle or invest their funds to unprofitable projects. Corporate governance is also related to how investor can control or monitor the manager.

Corporate governance is the system by which organizations are directed and controlled. It’s a set of relationships between company directors, shareholders and other stakeholder’s 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 also defined as an internal system encompassing policies, processes and people, which serve the needs of shareholders and other stakeholders, by directing and controlling management activities with good business savvy, objectivity, accountability and integrity (Mang’unyi, 2011).
The sacco sector is becoming increasingly important in Kenya. This sector is a key player in the economy, controlling about 43 per cent of Kenya’s gross domestic product (GDP) and yet few researchers have researched on a direct link between corporate governance and financial performance within this sector. The development of the sacco societies to offer ‘banking like’ services and expansion of the membership definition has brought additional risks to a hitherto conservative and closed bond Sacco industry. This increased and diverse membership driven by the bank like products has equally increased the systemic importance of the deposit taking saccos. The need to improve the financial soundness of the sacco subsector and ensure sound corporate governance explains the need of the prudential regulatory framework that SASRA is mandated to implement. The licensed deposit taking saccos are required to observe minimum operational regulations and prudential standards in the conduct of sacco business (Sacco Supervision Report, 2012).

Many studies have been carried out on corporate governance and firms’ performance within and without Kenya, but little has been done on sacco sector. In Kenya, the studies done in financial services sector have focused on other companies other than sacco sector. For instance, Jebet (2001) conducted a study of corporate governance practices among the quoted companies in Kenya, Muriithi (2005) did a study on the relationship between corporate governance mechanisms and performance of firms quoted on the NSE, Manyuru (2005) researched on corporate governance and organizational performance the case of companies quoted at the NSE while Matengo (2008) did a study on the

1.1.1 Corporate Governance

According to Mayer (1997), corporate governance is concerned with ways of bringing the interests of investors and managers into line and ensuring that firms are run for the benefit of investors. It is concerned in ways in which all stakeholders attempt to ensure that managers, employees and other insiders are always taking appropriate measures that safeguard their interests. Corporate governance is the system by which organizations are directed and controlled. It’s a set of relationships between company directors, shareholders and other stakeholder’s 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).

Metrick and Ishii (2002) define corporate governance as both the promise to repay a fair return on capital invested and the commitment to operate a firm efficiently given investment.

Corporate governance has also been defined by Keasey et al. (1997) to include the structures, processes, cultures and systems that engender the successful operation of organizations. The definition could therefore be centred on how the organization relates with other stakeholders within an environment. Maati (1999) viewed corporate governance as the whole set of measures taken within the social entity that is an enterprise to favour the economic agents to take part in the productive process, in order to generate some organizational surplus, and to set up a fair distribution between the partners, taking into consideration what they have brought to the organization. The Cadbury Committee, Cadbury (1992) defines corporate governance as the system by
which companies are directed and controlled. According to Shleifer and Vishny (1997), corporate governance is the ways in which suppliers of finance to corporations assure themselves of getting a return on their investment. Many studies on corporate governance have been looking into different ways in which investors can monitor their investments, where a board of directors serve as the liaison between investors and managers.

Corporate governance is important because it promotes good leadership within the corporate sector. Corporate governance has the following attributes; leadership for accountability and transparency, leadership for efficiency, leadership for integrity and leadership that respect the rights of all stakeholders (Institute of Corporate Governance of Uganda, 2000). Effective corporate governance is critical to firm performance and by extension shareholders’ value and especially so after the high profile corporate collapses and scandals such as Enron, Worldcom and others in the US, serving as an impetuous to such recent U.S. regulations as the Sabarnes-Oxley Act of 2002, considering the most sweeping corporate governance regulations in the past 70 years Byrnes et al.(2003), the main object of the Act being to protect investors by improving the accuracy and reliability of corporate disclosures made pursuant to the securities laws and other purposes. Others are Parmalat in Italy, Marcos10b & Fortune and Baby Doc of Haiti. Back in Kenya, the collapse of Kenya United Insurance, Lake Star Insurance, Goldenberg, Kenren and Anglo-Leasing scandal clearly point out on the need of good corporate governance. Corporate governance has succeeded in attracting a good deal of public interest because of its apparent importance for economic health of corporations and society in general. Corporate governance is about exercise of power over corporate entities. It has become one of the central issues in the running and regulation of modern
enterprise today. However the underlying ideas and concepts of corporate governance have been surprisingly slow to evolve.

Lack of sound corporate governance has enabled bribery, acquaintance and corruption to flourish and has suppressed sound and sustainable economic decisions. It is also important to remember that although corporate governance has emerged as a way to manage modern joint stock corporations it is equally significant in state-owned enterprises, cooperatives, and family businesses. Regardless of the type of venture, only good governance can deliver sustainable good business performance, Freeman (1984). Organizations with good corporate governance have the capacity to maintain high-quality services and to deliver improvement. Poor governance arrangements set the framework within which the organizational systems and processes fail to detect or anticipate serious service and financial failures. Baker (2007) Good governance in organizations, based on openness, clarity and honest accountability enhances public trust and civic engagement.

Corporate governance is a set of rules that define the relationship between stakeholders, management, and board of directors of a company and influence how that company is operating. At its most basic level, corporate governance deals with issues that result from the separation of ownership and control. But corporate governance goes beyond simply establishing a clear relationship between shareholders and managers. The presence of strong governance standards provides better access to capital and aids economic growth. Corporate governance also has broader social and institutional dimensions. Properly designed rules of governance should focus on implementing the values of fairness, transparency, accountability, and responsibility to both shareholders and stakeholders.
Good corporate governance ensures that the business environment is fair and transparent and that companies can be held accountable for their actions (Nicolaescu, 2012).

The main idea of this study was to examine whether or not the factors (independent variables) taken into consideration at this study could determine the effect of financial performance of saccos through corporate governance, those independent variables are Board size – number of board members within a financial year, Diversity (Gender) - number of women on the board, the compensation of the board- average compensation of all directors on the board, and the working experience of the board- number of years served in a board.

1.1.2 Financial Performance

A wide variety of definitions of firm performance have been proposed in the literature (Barney, 2002). For example, both accounting and market definitions have been used to study relationships between corporate governance, corporate social responsibility and firm performance (Orlitzky, Schmidt & Rynes, 2003). Conversely, stakeholder views regard firm performance as being the total wealth generated by the firm before distribution to the various stakeholders rather than the accounting profit allocated to the shareholders (Riahi-Belkaoui, 2003).

Firm performance is a subjective measure of how well a firm can use assets from its primary mode of business to generate revenues. There are many different ways to measure firms’ performance, but all measures should be taken in aggregation. These include accounting based measure such as return on assets (ROA), return on equity (ROE), accounting profits, earning per share (EPS), dividend pay-out and stock market
based measures such as Tobin Q. Measuring firms performance using accounting ratio is common in the Corporate governance literature Demaetz and Lehn, (1985), Ang et al. (2000), in particular, return on capital employed, return on assets and return on equity.

The study focused on using the Return on Asset (ROA) – Net Income divided by total assets which was the dependent variable as a measure of saccos financial performance.

1.1.3 Corporate Governance and Financial Performance

Various theories carry mixed literature concerning the relationship between corporate governance and financial performance. For example; according to the Agency theory there is conflict of interest between the principals who are the owners and the agents who have been appointed to run the organizations on behalf of the principal. The theory aims at resolving two problems that can occur in agency relationships. These problems arise due to conflict of interests between the principal and the agent, which arise due to separation of ownership and control which has been confirmed by Davis, et al. (1997), on the other hand stewardship theory holds that there is no conflict of interest between managers and owners, and that the goal of governance is precisely, to find the mechanisms and structure that facilitate the most effective coordination between the two parties (Donaldson, 1990). Stewardship theory assumes that managers are stewards whose behaviors are aligned with the objectives of their principals. According to the stakeholder theory, corporate governance is primarily concerned with how effective different governance systems are in promoting long term investment and commitment amongst the various stakeholders, (Williamson, 1985). Sundaram and Inkpen (2004) contend that stakeholder theory attempts to address the group of stakeholders deserving and requiring management’s attention.
The empirical literature shows that a lot of studies try to measure the corporate governance influence on financial performance and the literature has found conflicting relationship. Vafeas & Theodorou (1998), Brick & Chidambaran (2010) and Rashid et al. (2010) found no relationship between board independence and firm performance. Khan & Awan (2012) study reported a positive association between board independence and firm performance proxy by Tobin Q, return on asset and return on equity. Ameer et al. (2010) study also found a positive relationship between board independence and firm performance. Adams & Ferreira, (2009) found that women have better board meetings attendance than men; however they found gender to have a negative relationship on firm performance. Erhardt et al. (2003) finding was contradictory as they found a positive relationship between percentage of women on board and firm performance. Simpson et al. (2010) also suggested that board diversity through women representation has positive impact on firm performance through increased profitability and shareholders return. Nina et al. (2006) found a positive relationship between number of women on top management and firm performance but performance strongly depend on their qualifications.

1.1.4 Saccos Regulated by SASRA

The Sacco Societies Regulatory Authority (SASRA- The Authority) is a semi-autonomous government agency under the Ministry of Industrialization and Enterprise Development. It is a creation of the Sacco Societies Act 2008 and was inaugurated in 2009 charged with the prime responsibility to license and supervise deposit taking sacco
societies in Kenya, that is, those Saccos that operate Front Office Saving Activities (FOSA). By the 31st December 2013 the licensed deposit taking Saccos stood at 134.

SASRA was formed as part of the reforms that were being undertaken by the Government of Kenya in the financial sector with the objectives of protecting the interests of sacco members and ensuring that there is confidence in the public towards the sacco sector and spurring Kenya’s economic growth through the mobilization of domestic savings. The Authority derives its powers to regulate the deposit taking sacco societies in Kenya from the Sacco Societies Act 2008 and the Regulations issued there under, that is, the sacco society regulations.

Since inception the Authority has developed various regulatory and surveillance tools to ensure effective implementation of its legal mandate of licensing, supervising and regulating of Saccos. The Authority has also adopted a risk based supervision framework to further enhance its supervision capacity. It has continued to review saccos Information technology infrastructure to ensure they develop the required capacity to comply with regulatory requirements.

The Authority has put in place some minimum key requirements to ensure that there is proper governance in place within the sacco movement. According to the Authority, the supreme authority of a sacco society is to be exercised in general meetings, and members have the responsibility of ensuring that only credible members are elected to the board of directors, who should all be non-executive directors. The boards of directors’ have various responsibilities bestowed upon them by the regulator. These include; ensuring that the management maintains proper and accurate records that reflect the true and fair
position of the sacco society’s financial condition, ensuring that the sacco society functions effectively and that an adequate and effective internal control system is put in place and establishing appropriate policies including human resource policy, credit policy, investment policy, savings policy, liquidity policy, information preservation policy, dividend policy and risk management policy.

The Authority has also put a limit on the number and frequency of meetings that should be held by the board of directors in any given financial year. The number of meetings should not be more than twelve in any financial year and not more two months should lapse between the date of one meeting and the date of the next meeting. In addition all board of directors in saccos are expected to establish various board or management committees, including an audit and a credit committee as may be necessary to effectively discharge its functions. The audit committee should be duly constituted by the board of directors to review the financial conditions of the sacco society, its internal controls, performance and findings of the internal auditor and to recommend remedial actions at least once in every three months. The regulator requires that audit committee not to consist of not more than three members appointed from the board, one of whom shall be conversant with financial and accounting matters and the chairman of the board should not be a member of the audit committee.

The boards of directors’ are not expected to get any remuneration in form of salaries for services rendered to the sacco society, but may be reimbursed for necessary expenses incurred in course of discharging lawful duties to the benefit of the sacco society. No
member of the board is permitted to hold the position of a director in more than one sacco society licensed under the Act. The appointment and removal of the CEO of the Sacco is the responsibility of the board of directors, while on the other hand the CEO has the responsibility of ensuring that the board of directors is frequently and adequately appraised of the operations of the sacco society through presentation of relevant board papers. In addition all officers of the sacco are expected to comply with governance rules as prescribed by the Ethics Commission for Cooperative Societies established under Public Officer Ethics Act, 2003 (The Sacco Society Act, 2008).

1.2 Research Problem

Despite tight regulatory framework, corporate governance continues to weaken in Kenya (Mang’unyi, 2011). According to Muriithi (2009), many companies have been characterized by scandals. The introduction of corporate governance practices in the Sacco sector by SASRA in Kenya is aimed to provide a mechanism to improve investor confidence and trust in management and promote economic development of the country. However, efficiency of the corporate governance structures and practices on saccos operating in the highly competitive environment in Kenya has not been empirically investigated. Therefore, in order to understand the governance practices that contribute in enhancing the value of saccos regulated by SASRA, this study will aim at exploring the efficacy of corporate governance practices, which affect saccos performance resulting in accountability to shareholder and other stakeholders through appropriate corporate governance practices, which enhances the value of the saccos in Kenya.
The sacco sector is becoming increasingly important in Kenya. This sector is a key player in the economy, controlling about 43 per cent of Kenya’s gross domestic product (GDP) and yet few researchers have researched on a direct link between corporate governance and financial performance within this sector. This therefore called for an investigation into the effect of corporate governance on the financial performance of saccos in Kenya. This study aims at determining the effect of corporate governance on the financial performance of saccos regulated by SASRA in Kenya.

Many researches have been carried out on corporate governance and firms’ performance within and without Kenya, but little has been done on sacco sector. In Kenya, the studies done in financial services sector have focused on other companies other than sacco sector in Kenya. For instance, Jebet (2001) conducted a study of corporate governance practices among the quoted companies in Kenya, Muriithi (2005) did a study on the relationship between corporate governance mechanisms and performance of firms quoted on the NSE, Manyuru (2005) researched on corporate governance and organizational performance the case of companies quoted at the NSE while Matengo (2008) did a study on the relationship between corporate governance practices and performance: the case of banking industries in Kenya. The study will to answer the following question: What is the effect of corporate governance on the financial performance of saccos?

1.3 Research Objective

The objective of the study was to investigate the effect of corporate governance on the financial performance of saccos regulated by SASRA, whereas the specific objectives were to find out the effects of (independent variables) taken into consideration at this study on the financial performance of saccos regulated by SASRA. The objectives were;
to find out the effects of board size on the financial performance of saccos regulated by SASRA, to establish the effect of board diversity - as measured by the number of women in the board on financial performance of saccos regulated by SASRA, to establish the effect of boards’ compensation on the financial performance of saccos regulated by SASRA, and to establish the effect of boards level of experience as measured by the number of years served in the board on the financial performance of saccos regulated by SASRA.

1.4 Value of the Study

1.4.1 Scholars and Academicians

The study may be important to scholars and academicians by adding to body of existing knowledge on corporate governance. The study will also give recommendation for further researchable areas that will be useful in furthering the understanding of financial performance and corporate governance.

1.4.2 Management

It is expected that the findings of this study will be of interest to the management of saccos who will be able to determine the effects of corporate governance on the value of their saccos and make prudent decisions on governance improvement.

1.4.3 Investors

The study is expected to provide valued information that investors can use to make investment decisions.
1.4.4 Policy Makers– SASRA

The policy makers would obtain knowledge of the various firm dynamics and the responses that are appropriate; they will therefore obtain guidance from this study in designing appropriate regulations and policies of governance structure saccos in Kenya.
CHAPTER TWO: LITERATURE REVIEW

2.1 Introduction

A substantial number of studies have attempted to develop theoretical and empirical works to understand the relationship between corporate governance and the financial performance of firms’. This chapter reviews the theories that relate to corporate governance mainly focusing on Agency theory, Stewardship theory and Stakeholders’ theory, the empirical studies on corporate governance and the financial performance of firms’ and finally provides a summary of the literature review.

2.2 Theoretical Review

2.2.1 Agency Theory

According to Jensen & Meckling (1976), Agency theory is directed on an agency relationship, in which one party (the principal) appoints another party (the agent), to perform their work. This kind of relationship is described by agency theory in terms of a contract. The directors or managers who are the shareholder’s agents are given the responsibility of running the business by the shareholders (Clark, 2004). The agents are expected to act and make decisions on the best interest of the principal (Padilla, 2000). Agency theory aims at resolving two problems that can occur in agency relationships. These problems arise due to conflict of interests between the principal and the agent, which arise due to separation of ownership and control which has been confirmed by Davis, et al. (1997).
Managers tend to develop opportunistic behavior due to legitimacy authority that has been bestowed to them by the shareholders, this behavior leads to conflict of interest causing agency problem. In Agency theory, despite the agent being given the decision making authority by the principal the agent will not always act in the best interest of the principals. The principal has to control or restrain the behaviour of the agent for his interest to be pursued. The principal will try to achieve controls through monitoring activities or task. To minimize the potential for such agency problems, Jensen (1983) recognizes two important steps: first, the principal-agent risk-bearing mechanism must be designed efficiently and second, monitoring costs are incurred through performance measuring, observing and controlling the actions of the principals. These costs include performance based incentives like bonuses, cost of dismissal, cost of audit reports, corporate reports and cost of compliance. The agent incurs bonding costs which include cost of additional information disclosure to shareholders. Agent stops incurring bonding cost when marginal reduction in monitoring cost equals marginal increase in bonding costs (Jensen & Meckling, 1976)

The principal expect to be compensated if the agent takes action that might harm his investment. For example, if the board of directors who are the agent made decision to invest in more risky project, the shareholders will demand to be compensated thus increasing the cost of capital. It is therefore a challenge to align the interest of principal and the agent due to the following areas of conflict; moral threat, earnings retention, time horizon and risk perception and which can be referred as agency problems (Jensen & Meckling, 1976; Shleifer & Vishny, 1989). The model of an employee portrayed in the
agency theory is more of a self-interested, individualistic and are bounded rationality where rewards and punishments seem to take priority (Jensen & Meckling, 1976).

2.2.2 Stewardship Theory

Donaldson & Davis (1991&1993) developed Stewardship Theory as a new perspective to understand the existing relationships between ownership and management of the company. The theory holds that there is no conflict of interest between managers and owners, and that the goal of governance is precisely, to find the mechanisms and structure that facilitate the most effective coordination between the two parties (Donaldson, 1990). Stewardship theory assumes that managers are stewards whose behaviors are aligned with the objectives of their principals.

According to Davis et al. (1997), where a steward is faced with objectives that are conflicting with those of the stakeholder, he will make decision that will be for the best interest of the group. The decision will improve organisation performance which will generally satisfy the whole group. The actions of the stewards’ are based on the belief that by pursuing organisation objectives the shareholders will be satisfied and their own personal needs will be met eventually. The level of motivation from operating work environment normally determines the steward’s performance. Managers are conceived as being motivated by a need to achieve, to gain intrinsic satisfaction through successfully performing inherently challenging work, to exercise responsibility and authority, and thereby to gain recognition from peers and bosses. Therefore, there are non-financial motivators for managers, (Donaldson, 2008).
Since the steward is motivated and can be trusted the principal can save on monitoring and bonding cost and incentives (Davis et al. 1997). If the shareholders attempts to introduce controls, this will be counter productive to the stewards since their objectives are already aligned to those of the organisation. A steward protects and maximizes shareholders' wealth through firm performance, because, by so doing, the steward's utility functions are maximized. Risk averse principals will take agency governance while risk neutral principals will prefer stewardship governance.

2.2.3 Stakeholders Theory

Wheeler et al. (2002) argued that stakeholder theory was derived from a combination of the sociological and organizational disciplines. The theory is concerned with value and beliefs about the appropriate relationships between the individual, the enterprise, and the state. It involves a discourse on the balance of responsibilities, accountability, and power throughout the society. It is not a predictive theory that can be researched. Consequently, this societal view of corporate governance is probably better thought as a philosophy rather than a theory. Blair (1995) defined stakeholders to be those actors who have contributed firm specific assets. Donaldson & Preston (1995) provided the following definition ‘Stakeholders are identified through the actual or potential harms and benefits that they experience or anticipate experiencing as a result of the firm's actions or inactions’. Stakeholders are described by Turnbull (1997) as 'strategic stakeholders' as strategic issues concern the ability of a firm to exist.

Stakeholder theory can be defined as any group or individual who can affect or is affected by the achievement of the organization’s objectives. Stakeholder theorists
suggest that managers in organizations have a network of relationships to serve – this include the suppliers, employees and business partners. And it was argued that this group of network is important other than owner-manager employee relationship as in agency theory. On the other end, Sundaram & Inkpen (2004) contend that stakeholder theory attempts to address the group of stakeholders deserving and requiring management’s attention.

According to the stakeholder theory, corporate governance is primarily concerned with how effective different governance systems are in promoting long term investment and commitment amongst the various stakeholders, (Williamson, 1985). Kester (1992), for example, states that “the central problem of governance is to devise specialized systems of incentives, safeguards, and dispute resolution processes that will promote the continuity of business relationships that are efficient in the presence of self-interested opportunism”. Blair (1995) also argued that corporate governance should be regarded as the set of institutional arrangements for governing the relationships among all of the stakeholders that contribute firm specific assets. Companies stakeholders argue that, companies owe a duty to all those affected by their behavior. This calls for even directors to be accountable and responsible to a wide range of stakeholders far beyond companies’ current company law responsibility to shareholders.

Such responsible behaviour, the stakeholder advocate argue, should be the price society demands from companies for the privilege of incorporation, granting shareholders limited liability for the company’s debts.
Stakeholder theory was criticized by Jones & Wicks (1999), for assuming a single-valued objective (gains that accrue to a firm’s constituencies). It was pointed out that the performance of a firm is not and should not be measured only by gains to its stakeholders. There are other key issues which are critical and should be considered such as flow of information from senior management to lower ranks, inter-personal relations, working environment, etc. An extension of the theory called enlightened stakeholder theory was proposed. However, problems relating to empirical testing of the extension have limited its relevance.

2.3 Determinants of Firms Financial Performance

Financial performance in saccos can be said to be a subjective measure of how well a sacco can use assets from its primary mode of business to generate revenues. A sacco financial performance is directly influenced by its market position, that is, how well a Sacco has positioned itself in the market in terms of common bond. A common bond is a group of clientele with common objective or who undertake similar business who have come together to form the sacco, for example dairy farmers, players of a given industry such as banking who have formed Kenya bankers sacco. The number of members in a sacco also influences its performance. Saccos with large membership are able to mobilize savings which is advanced to members in form of loans, which is the core business of many sacco. The sacco is therefore able to grow its loan portfolio which plays a great role in interest income of the sacco. Risk is another important factor that influences the saccos financial performance. The level of risk exposure can cause changes in its market value. Economic growth is another component that helps to achieve a better position in the eyes of the investors who are the members, because investors also take into
consideration expected future profits. The size of the sacco can have a positive effect on financial performance because larger saccos can use this advantage to get some financial benefits in business relations. Large saccos have easier access to the most important factors of production, including human resources. Also, large saccos often get cheaper funding. Leverage also has an influence on saccos performance. According to Barton & Gordon (1988) entities with higher profit rates will remain low leveraged because of their ability to finance their own sources. On the other hand, a high degree of leverage increases the risk of bankruptcy of Saccos. Total assets are considered to positively influence the saccos financial performance, assets greater meaning less risk.

2.4 Empirical Studies

Research on good corporate governance practices, especially the research that relates good corporate governance practice and firm performance has been widely done both locally and internationally.

Locally several studies have been done on corporate governance and firms performance. Ngugi (2007) did a study on the relationship between corporate governance structures and the performance of insurance companies in Kenya. He found out that the effectiveness of a board depends on the optimal mix off inside and outside directors. The study also found out that inside directors are more familiar with the firm’s activities and they can act as monitors to top management especially if they perceive the opportunity to advance into positions held by incompetent executives. He concluded that an optimal board composition leads to better performance of the companies.
Lishenga (2011) investigated how corporate governance and practices of firms at the NSE change as remedial action to persistent fall in financial performance. The population of his study was all listed firms in the NSE from 1998 to 2004. He grouped his population into winners for companies with persistent decline in financial performance and mixed depending on change in direction of company financial performance value that is appreciating or declining. Data analysis was via descriptive statistics by testing the significance difference in means between the three groups. He found out that the board meeting frequency increase with decline performance and finally CEO remuneration has nothing to do with a firm’s performance. He concluded that companies respond to declining firm performance by changing governance structure and practices in diverse ways. The study suggested that there is no optimal governance structure that exists hence the optimal governance structure depends on different firms or market segments.

Mang’unyi (2011) carried out a study to explore the ownership structure and corporate governance and its effects on performance of firms. The population of his study was banks operating within Nairobi city in Kenya. In the study a stratified sampling methodology was used where 40 banks were selected. Semi structured questionnaires which were administered to selected bank managers were used to collect data and the analysis was done using descriptive method with the help of SPSS analysis tool that was used to compute frequencies and percentages and the hypothesis tested using one way ANOVA. His study revealed that there was significant difference between corporate governance and financial performance of banks. The study recommended that corporate entities should promote corporate governance to send positive signals to potential
investors and those regulatory agencies including the government should promote and socialize corporate governance and its relationship to firm performance across firms.

Kerich (2006) after undertaking a study on corporate governance structures and performance in firms quoted in the NSE observed that there is a positive relationship between the listed firms and financial performance and frequency of board meetings, the ratio of outside directors, percentage of insider ownership and the executive compensation. In his study he used cross sectional survey design that sought to identify differences in governing structures when experiencing under performance. The population of the study was all 47 listed firms on the NSE for the period of five years from 2000 to 2005. The data analysis was done suing two approaches, where descriptive statistics were computed for the winners and losers over the test period for all governance variables and to cross check the conclusion that was arrived at on the statistics regression analysis was used.

Ongore and K’Obonyo (2011) conducted a study to examine the interrelations among ownership, board and manager characteristics and firm performance in a sample of 54 firms listed at the Nairobi Securities Exchange. His study showed a positive relationship between managerial discretion and performance. However, the relationship between ownership concentration and government on firm performance was significantly negative.

Rogers (2006) conducted a study on corporate governance and financial performance of selected commercial bank in Uganda. The study explores the relationship between the
core principles of corporate governance and financial performance in commercial banks of Uganda. Finding indicates that corporate governance predicts 34.5% of the variance in the general financial performance of commercial banks in Uganda. However the significant contributors on financial performance include openness and reliability. Openness and reliability are measures of trust. On the other hand credit risk as a measure of disclosure has a negative relationship with financial performance. It was obvious that trust has a significant impact on financial performance; given that transparency and disclosure boosts the trustworthiness of commercial banks. It's recommended that banks both local and international should enforce full disclosure practices and transparency practices thereby enhancing trust in order to survive in the competitive financial landscape.

Brown & Caylor (2004) conducted a study on corporate governance and firm performance. The study examined whether firms with weaker corporate governance perform more poorly than firms with stronger corporate governance and they found that firms with weaker corporate governance perform more poorly. They also, examined whether those firms that have weaker corporate governance are less profitable than firms with stronger corporate governance. They found that firms with weaker corporate governance are less profitable. They also examined if firms with weaker corporate governance are riskier and pay out fewer dividends, than firms with stronger corporate governance, it was found firms with weaker corporate governance tend to be riskier and have lower dividend payouts and lower dividend yields than those firms with stronger corporate governance. Finally, they examined which of the four corporate governance factors considered by Institutional Shareholder Services (ISS) is the driving factor of their
results. The four factors they examined are board composition, compensation, takeover defenses, and audit. They identified that the Board composition is the most important factor and that the least important factor is takeover defenses.

Chiang (2005) conducted a study on corporate governance and corporate performance. The study explored the relationship among indicators of corporate governance, including transparency and operating performance measures, and whether or not the indicators could be predictors of operating performance. The study supplemented Standard & Poor criteria with information gathered from all public materials in order to obtain more comprehensive transparency information. His results indicated that corporate transparency had a significant positive relationship with operating performance. His study concluded that companies with good corporate governance also had a significant positive relationship with operating performance.

Bocean & Barbu (2005) conducted a study on corporate governance and firm performance. The purpose of the study was to develop the understanding of corporate governance and its effects on corporate performance and economic performance. In doing so, it addressed some of the underlying factors that promote efficient corporate governance, and examined some of the economic implications associated with various corporate governance systems. The study provides a framework for understanding how corporate governance can affect corporate performance. It was found that corporate governance matters for economic performance, insider ownership matters the most, outside ownership concentration destroys market value, direct ownership being superior to indirect. Three main approaches to firm level performance were found in social science research: research based on market prices, accounting ratios and total factor profitability.
Finally, measuring performance by Tobin’s Q and operationalizing it as market to book is consistent with agency theory and the study found that large outside owners destroy market value, while inside owners create it unless the stakes are unusually big, and that direct ownership is more beneficial than indirect.

Klapper & Love (2002) also found that there was a positive relation between corporate governance and firm performance that was measured with ROA and Tobin’s Q. Beside, CheHaat et al. (2008) found that corporate governance mechanisms have a significant influenced on firm market performance (Tobin’s Q). However, some research found that there was no relation between corporate governance with the company performance (for example Labelle, 2002 & Raffournier, 1995).

In Indonesia, the issue of good corporate governance and its relation to firm performance has been investigated by several researchers. Darmawati et al. (2005) found that the practice of good corporate governance was not significantly influenced towards the firm market performance as measured by Tobin’s Q, but significantly influenced the firm’s operating performance (as measured by ROE). Based on the above discussion, it can be convinced that the implementation of good corporate governance is certainly an important element.

Gompers et al. (2003), Marry & Stangeland (2003), Klapper & Love (2004), and Bauer et al. (2003) examine the impact of the governance standards on firm performance approximated by profitability ratios as well. All of them document a positive relationship between governance scorecard and performance except for Bauer et al. (2003) who surprisingly detect a significant negative relationship.
2.5 Summary of the Literature Review

Good corporate governance is of importance in all organizations. It is argued that good corporate governance sets the ‘Tone at the Top’ which in turn impacts what transpires at the lower levels in the organization. The presence of an effective corporate governance system within the sacco sector in Kenya helps provide a degree of confidence that is necessary for the proper functioning of the entire sacco sector and enhance financial performance.

Based on the various literature review the effect of good corporate governance practices on financial performance is not consistent and vary with the firms and dimensions of corporate governance adopted. Some studies have shown positive correlation while others like Heracleous (2001) arguing that corporate governance best practices are not associated with higher performance.

From the empirical evidence it is clear that a lot of studies have been conducted with respect to the relationship between corporate governance and firms’ performance. In the Kenyan context however not very many studies have been done relating to the sacco sector. Many researchers have put great attention to banking and other service industries thereby ignoring other sectors like sacco sector which are still prone to corporate governance issues despite the fact that all sectors are important player in Kenya’s economy. The literature review therefore presents a strong justification towards addressing the knowledge gap on relevant study of the sacco sector in Kenya. This paper
therefore intends to take a different approach and study a sample of deposit taking saccos regulated by SASRA.
CHAPTER THREE: RESEARCH METHODOLOGY

3.1 Introduction

This chapter explains the methods that were used by the study to fulfill its set objectives. It captures the research design, a description of the population and sample, data collection and data analysis.

3.2 Research Design

This study adopted a descriptive research design. According to Mugenda and Mugenda (2003), descriptive research is a process of collecting data in order to test hypotheses or to answer questions concerning the current status of the subjects in the study. A descriptive study determines and reports the way things are.

3.3 Population

The target population of this study was all deposit taking saccos regulated by SASRA as at December 2013. By 31st December 2013 the licensed deposit taking saccos stood at 130.

3.4 Sample

The sample for the study was 24 saccos. These are all deposit taking saccos regulated by SASRA at 2013 which are situated within Nairobi.

3.5 Data Collection

The study used secondary data for analysis. The information of most deposit taking saccos regulated by SASRA are normally in the public domain and the data was obtained from the Authority. The period of the study was from 2009-2013.
3.6 Data Analysis

The study used multivariate regression model to determine the relationship between the dependent and the independent variables. The dependent variable in the study was the Return on Assets (ROA) – Net income divided by average total assets while the independent variables were Board size – the total number of board members serving within a financial year, Diversity (Gender) - The number of women serving on the board within a financial year, the compensation of the board- average compensation of all directors on the board, and the working experience of the board- number of years served in a board. The control variables will be Firm size - natural logarithm of book value of total assets and Firm age - natural logarithm of years since establishment. The multivariate regression model for this study was;

\[ Y = A + B_1X_1 + B_2X_2 + B_3X_3 + B_4X_4 + B_5X_5 + B_6X_6 \]

Where;

\[ Y = \text{Return on Assets - Net Income divided by total assets} \]

\[ A = \text{Constant} \]

\[ X_1 = \text{Board size – The total number of board members serving within a financial year} \]

\[ X_2 = \text{Diversity (Gender) – The number of women serving on the board within a financial year} \]

\[ X_3 = \text{Compensation of the board - Average compensation of all directors on the board; natural logarithm will be taken after adding 1 to all firms to control firms that don’t pay compensation} \]
X4= Working experience of the board - Number of years served in a board.
X5= Firm size - Natural logarithm of book value of total assets
X6= Firm age - Natural logarithm of years since establishment

For interpretation purposes the study employed descriptive statistics such as mean scores, standard deviation and variance. A change in Y (dependent variable) depends on changes in Xn (independent variables).

The study used Statistical package for Social Sciences-SPSS version 22, that aided in data analysis.

3.7 Test of Significance

The Pearson product moment coefficient (R) was used to establish the association between the variables (Financial performance and corporate governance) based on the population data. A coefficient of determination (R²) was performed to determine how much of the dependent variable comes about as a result of the independent variable being tested. The study tested R² at 95% significance level. To test the significance of the findings, analysis of variance (ANOVA) was done.
CHAPTER FOUR: DATA ANALYSIS, RESULTS AND DISCUSSIONS

4.1 Introduction

This chapter presents analysis and findings of the study as set out in the research methodology. The study findings are presented on the effects of corporate governance on the financial performance of deposit taking saccos regulated by SASRA. The data was gathered exclusively from saccos’ financial statements and SASRA regulation reports that were obtained from SASRA office using the data collection form as the research instrument. The data collection form was designed in line with the objectives of the study.

4.2 Descriptive Statistics

This section explains the characteristics of corporate governance factors that affect the financial performance of deposit taking saccos regulated by SASRA.
Table 4.1: Descriptive statistics

<table>
<thead>
<tr>
<th>YEAR: 2009-2013</th>
<th>Y</th>
<th>X1</th>
<th>X2</th>
<th>X3</th>
<th>X4</th>
<th>X5</th>
<th>X6</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mean</td>
<td>0.0291</td>
<td>8.9583</td>
<td>1.8500</td>
<td>7.7215</td>
<td>6.8333</td>
<td>9.9593</td>
<td>1.5363</td>
</tr>
<tr>
<td>Standard Error</td>
<td>0.0061</td>
<td>0.1646</td>
<td>0.2237</td>
<td>0.1062</td>
<td>0.3223</td>
<td>0.1112</td>
<td>0.0297</td>
</tr>
<tr>
<td>Median</td>
<td>0.0234</td>
<td>9.0000</td>
<td>2.0000</td>
<td>7.6797</td>
<td>7.0000</td>
<td>9.8328</td>
<td>1.5854</td>
</tr>
<tr>
<td>Standard Deviation</td>
<td>0.0297</td>
<td>0.8065</td>
<td>1.0958</td>
<td>0.5201</td>
<td>1.5788</td>
<td>0.5445</td>
<td>0.1457</td>
</tr>
<tr>
<td>Sample Variance</td>
<td>0.0009</td>
<td>0.6504</td>
<td>1.2009</td>
<td>0.2706</td>
<td>2.4928</td>
<td>0.2965</td>
<td>0.0212</td>
</tr>
<tr>
<td>Kurtosis</td>
<td>7.8306</td>
<td>10.1802</td>
<td>0.4033</td>
<td>0.9436</td>
<td>-0.5186</td>
<td>-0.6907</td>
<td>4.2864</td>
</tr>
<tr>
<td>Skewness</td>
<td>2.5586</td>
<td>1.7066</td>
<td>0.3090</td>
<td>-0.0690</td>
<td>-0.0629</td>
<td>0.1806</td>
<td>-2.1314</td>
</tr>
<tr>
<td>Minimum</td>
<td>0.0038</td>
<td>7.0000</td>
<td>0.0000</td>
<td>6.4029</td>
<td>4.0000</td>
<td>9.0986</td>
<td>1.0792</td>
</tr>
<tr>
<td>Maximum</td>
<td>0.1389</td>
<td>12.0000</td>
<td>4.0000</td>
<td>8.7362</td>
<td>10.0000</td>
<td>11.0061</td>
<td>1.7076</td>
</tr>
</tbody>
</table>

**Source: Research Findings**

The results showed that the board size had a mean of 8.9583 with a minimum of 7.0, a maximum of 12, skewness of 1.7066 and kurtosis of 10.180. Board diversity had a mean of 8.9583, minimum of 0, maximum of 4, skewness of 0.3090 and kurtosis of 0.4033. Compensation of the board had a mean of 7.7214, minimum of 6.4029, maximum of 8.7362, skewness of -0.069 and kurtosis of 0.9436. Board level of experience had a mean of 6.833, minimum of 4.0, maximum of 10.0, skewness of -0.0629 and kurtosis of -
Firm size had a mean of 9.9593, minimum of 9.0986, maximum of 11.006, skewness of 0.1806 and kurtosis of -0.691. Firm age had mean of 1.5363, minimum of 1.7076, maximum of 1.7076, skewness of -2.131 and kurtosis of 4.2864. Overall ROA had a mean of 0.0291, minimum of 0.0038, maximum of 0.1389, skewness of 2.5586 and kurtosis of 7.8306.

Analysis of skewness shows that board size, and firms size are asymmetrical to the right, while compensation of the board, working experience of the board and firms age are asymmetrical to the left. Additionally, board size and firms’ age is highly peaked compared to other regressors.

**4.3 Correlation Analysis**

After the descriptive analysis, the study conducted Pearson correlation analysis to indicate a linear association between the predicted and explanatory variables or among the latter. It, thus, help in determining the strengths of association in the model, that is, which variable best explained the relationship between corporate governance and financial performance as measured ROA.
Table 4.2: Correlation Matrix

<table>
<thead>
<tr>
<th></th>
<th>ROA</th>
<th>Board size</th>
<th>Diversi ty</th>
<th>Comp ensation of the board</th>
<th>Work ing experience</th>
<th>Firm size-Log of assets</th>
<th>Years-natural log</th>
</tr>
</thead>
<tbody>
<tr>
<td>ROA</td>
<td>Pearson Correlation</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Board size</td>
<td>Pearson Correlation</td>
<td>-0.2249</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Divers ity</td>
<td>Pearson Correlation</td>
<td>0.1326</td>
<td>0.0910</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Comp the board</td>
<td>Pearson Correlation</td>
<td>0.3687</td>
<td>0.2152</td>
<td>-0.3536</td>
<td>1</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Work ing experi ence</td>
<td>Pearson Correlation</td>
<td>-0.0346</td>
<td>0.165</td>
<td>-0.0402</td>
<td>0.1411</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>Firm size-Log of assets</td>
<td>Pearson Correlation</td>
<td>0.3803</td>
<td>0.3185</td>
<td>-0.1573</td>
<td>0.9191</td>
<td>0.0046</td>
<td>1</td>
</tr>
<tr>
<td>Years-natural log</td>
<td>Pearson Correlation</td>
<td>0.0946</td>
<td>0.1202</td>
<td>-0.1971</td>
<td>0.5493</td>
<td>-0.0688</td>
<td>0.5667</td>
</tr>
</tbody>
</table>

Source: Research Findings

From the Table 4.2, it can be deduced that there was a negative correlation between ROA and board size and working experience given a correlation value of -0.2249 and -0.0346 respectively, board diversity, compensation of the board, firm size and age of the firm showed a positive correlation with RAO. Board diversity had a correlation value of 0.1326 with compensation of the board having a correlation value of 0.3687. Firm size and age of the firm had correlation value of 0.3803 and 0.0946 respectively.
4.4 Regression Analysis

The regression method used for this study was the least square method. This was used to determine the line of best fit for the model through minimizing the sum of squares of the distances from the points to the line of best fit. Through this method, the analysis assumed linearity between the dependent variable and the independent variables.

Table 4.3: Regression Model Summary

<table>
<thead>
<tr>
<th>Regression Statistics</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Multiple R</td>
<td>0.6156</td>
</tr>
<tr>
<td>R Square</td>
<td>0.3789</td>
</tr>
<tr>
<td>Adjusted R Square</td>
<td>0.3160</td>
</tr>
<tr>
<td>Std. Error</td>
<td>0.02722</td>
</tr>
</tbody>
</table>

Source: Research Findings

The model had a Correlation value of 0.6156 which depicts good linear relationship between predicted and explanatory variables. The model was also moderately strong owing to R-square values of 0.3789 which was adjusted for errors to 0.3160. This depicts that the independent variables explains only 31.6% of the changes in financial performance as measured by ROA.
Table 4.4: Analysis of Variance (ANOVA)

<table>
<thead>
<tr>
<th>Source</th>
<th>Sum of Squares</th>
<th>df</th>
<th>Mean Square</th>
<th>F</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Regression</td>
<td>0.0077</td>
<td>6</td>
<td>0.00128</td>
<td>1.7287</td>
<td>0.1748</td>
</tr>
<tr>
<td>Residual</td>
<td>0.0126</td>
<td>17</td>
<td>0.0007</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>0.0203</td>
<td>23</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: Research Findings

Analysis of Variance’s (ANOVA) f-test was used to make simultaneous comparisons between two or more means; thus, testing whether a significant relation exists between variables (dependent and independent variables); thus, helping in bringing out the significance of the regression model. Table 4.4.2 presents f-value 1.7287 at significance value of 0.1748 (p < .05). It can be concluded that the regression model was insignificant.
Table 4.5: Regression Coefficient

<table>
<thead>
<tr>
<th></th>
<th>Coefficients</th>
<th>Standard error</th>
<th>T Stat</th>
<th>P-Value</th>
<th>Lower 95%</th>
<th>Upper 95%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Intercept</td>
<td>-0.1289</td>
<td>0.1155</td>
<td>-1.1160</td>
<td>0.2800</td>
<td>-0.3727</td>
<td>0.1148</td>
</tr>
<tr>
<td>Board size</td>
<td>-0.01502</td>
<td>0.0079</td>
<td>-1.9056</td>
<td>0.07375</td>
<td>-0.03164</td>
<td>0.00161</td>
</tr>
<tr>
<td>Diversity</td>
<td>0.0088</td>
<td>0.0064</td>
<td>1.37975</td>
<td>0.1855</td>
<td>-0.00464</td>
<td>0.0222</td>
</tr>
<tr>
<td>Compensation of the board</td>
<td>0.0235</td>
<td>0.0368</td>
<td>0.6395</td>
<td>0.5310</td>
<td>-0.0541</td>
<td>0.1011</td>
</tr>
<tr>
<td>Working experience</td>
<td>-0.0005</td>
<td>0.0041</td>
<td>-0.1221</td>
<td>0.9042</td>
<td>-0.0091</td>
<td>0.0081</td>
</tr>
<tr>
<td>Firms size – log of assets</td>
<td>0.0156</td>
<td>0.0344</td>
<td>0.4535</td>
<td>0.6559</td>
<td>-0.05700</td>
<td>0.0882</td>
</tr>
<tr>
<td>Years – Natural log</td>
<td>-0.03730</td>
<td>0.0480</td>
<td>-0.77657</td>
<td>0.4481</td>
<td>-0.1386</td>
<td>0.0640</td>
</tr>
</tbody>
</table>

Source: Research Findings

From the data in the above table the established regression equation was

$$ Y = -0.1289 - 0.01502X_1 + 0.0088X_2 + 0.0235X_3 - 0.005X_4 + 0.0156X_5 - 0.03730X_6 $$

4.5 Discussion of Findings

In summary, this study found that implementation of proper corporate governance is an important element in the financial performance of saccos. From the regression equation it was revealed that corporate governance measures that is; the Board size, number of board meetings, diversity (Gender), the compensation of the board, ownership of the board, the
working experience of the board, and the control variables which are sacco size and sacco age to a zero constant, the financial performance of saccos as measured by RAO will be -0.1289. The results also show that board size, working experience of the board and the age of the Sacco negatively affects saccos financial performance, while board diversity, compensation of the board and the size of the sacco affects financial performance positively. A unit increase in board size leads to decrease in financial performance by a factor of 0.01502, unit increase in diversity leads to increase of financial performance by factor 0.0088, unit increase in compensation of the board leads to increase of financial performance by factor 0.0235 and a unit increase of working experience of the board leads to a decrease in financial performance by factor 0.005. A unit increase in the size of the sacco leads to an increase in financial performance by factor 0.0156, while a unit increase in age of the sacco leads to a decrease in financial performance by factor 0.0373. At 5% level of significance and 95% level of confidence, board size had a 0.0738 level of significance; compensation of the board showed a 0.5310 level of significance, firm size had a 0.6559 level of significance, working experience had a 0.9042 level of significance, while firm age showed 0.4481 level of significance hence the most significant factor is board size. Overall board size had the greatest effect on the financial performance of deposit taking saccos, followed by firm age, then compensation of the board, followed by the firm size with working experience having the least effect to the financial performance of saccos. All the variables were insignificant (p>0.05).

Corporate governance has positive relation with financial performance hence the introduction of various governance policies will improve the financial performance and
performance efficiency. Many different claims by different authors explaining the impact of corporate governance on financial performance of firms in financial sector such as banks, MFIs and insurance companies have been explored and analyzed vis-à-vis the findings of the study. Competing explanations to the various arguments have also been shown. It was not, however possible to confirm the relationship between financial performance and some of the prepositions because of lack of relevant comparative data from other groupings of firms not within the financial sector. Future work should attempt to explore the linkages between transparency, communication, and performance in more depth and by use of different techniques.
5.1 Introduction

The chapter provides the summary of the findings from chapter four, and it also gives the conclusions and recommendations of the study based on the objectives of the study. The objectives of this study were to investigate the effects of corporate governance on the financial performance of deposit taking saccos regulated by SASRA.

5.2 Summary of findings

In summary the study found board diversity, compensation and size affects the financial performance of deposit taking saccos positively. From the regression analysis, board size, experience and firms age were found to negatively affect the financial performance of saccos.

A negative correlation was found between ROA and board size and working experience given a correlation value of -0.2249 and -0.0346 respectively, board diversity, compensation of the board, firm size and age of the firm showed a positive correlation with RAO. Board diversity had a correlation value of 0.1326 with compensation of the board having a correlation value of 0.3687. Firm size and age of the firm had correlation value of 0.3803 and 0.0946 respectively.

The study found a negative relationship between the number of board members and saccos’ financial performance. It is therefore important to ensure that there should not be
too many members on the board because a larger board’s size will contribute negatively to firm’s performance.

Increase in number of women on board leads to increase in saccos’ performance. Board should appoint female board members because these females will make a significant contribution to firm’s performance.

The outcomes from this study also indicate that board’s compensation will positively contribute to firm’s performance. As a result, it is necessary for saccos to consider an appropriate and competitive compensation level of board’s members. The compensation will provide a better link between shareholders and firm’s management and this link will enhance firm’s performance to maximize shareholders’ value.

5.3 Conclusion

From the findings on the effects of diversity, compensation and size on the financial performance of deposit taking saccos, the study found that these aspects affect the financial performance of saccos positively. From the regression analysis, board size, experience and firms age were found to negatively affect the financial performance of saccos.

The outcomes from this study also indicate that board’s compensation will positively contribute to firm’s performance. The study thus concludes that compensation of the board positively influence the financial performance of deposit taking saccos.
Female board members represent a diversification of board’s membership and this diversified nature will contribute positively to saccos’ financial. Thus the study concludes that diversity in the board positively influence the financial performance of deposit taking saccos. to great extent.

The study found out that size influences the financial performance of deposit taking saccos. It was established that size of the sacco positively influenced the financial performance of deposit taking saccos. The study thus concludes that size of the firm positively influence the financial performance of deposit taking saccos.

The study also found out board size, working experience and age of the Sacco negatively influenced the financial performance of deposit taking saccos. The study thus concludes that board size, working experience and age of the firm negatively influence the financial performance of deposit taking saccos.

5.4 Policy Recommendation

This study aims to provide empirical evidence for saccos in enhancing their understanding in relation to the development of a corporate governance mechanism. As a result, saccos are now provided with evidence to set up flexible, dynamic and efficient corporate governance.

The study recommends that the board size, diversity and compensation be considered since they affect the financial performance of the deposit taking saccos. In particular, this study finds that female board members represent a diversification of board’s membership
and this diversified nature will contribute positively to saccos’ financial performance. Board should appoint female board members because these females will make a significant contribution to firm’s performance.

The study found that size of the board is another factor that affects financial performance. It therefore recommends that, there should not be too many members on the board because a larger board’s size will contribute negatively to firm’s performance. A large board makes decision making process to be slow and hence critical decision may take too long to be passed, and by the time they are passed it may be too late to realize the benefits.

The outcomes from this study also indicate that board’s compensation will positively contribute to firm’s performance. As a result, it is necessary for saccos to consider an appropriate and competitive compensation level of board’s members. The compensation will provide a better link between shareholders and firm’s management and this link will enhance firm’s performance to maximize shareholders’ value.

The study also recommends to the government through the Authority - SASRA to use the level of corporate governance existing in saccos as a basis of promotion

5.5 Limitations of the Study

The study encountered the challenge of confidentiality with regard to disclosure of information on saccos from the Authority (SASRA). The Authority was apprehensive when it came to divulging of information which it considered confidential. The
researcher surmounted the challenge by way of assuring them that the study was purely academic and their identity and those of the saccos they were affiliated to would always remain confidential. This aided them to freely give out the information.

The researcher encountered problems of time as the research was being undertaken in a short period with limited time for doing a wider research. However, the researcher countered the limitation by carrying out the research across the saccos that were selected which enabled generalization of the study findings on the effects of corporate governance and the financial performance of the deposit taking saccos in Kenya.

Finally, findings generated as a result of the study are not in themselves all conclusive as the study focused only on six corporate governance attributes determined necessary for the study by the researcher. Also, availability of data determined the elements for the study and not any statistical or probabilistic criterion. Hence, caution should be exercised in generalizing the results.

5.6 Suggestions for Further Studies

The area of education related to corporate governance’s knowledge and levels of financial performance offers opportunities for additional research. The study proposes that further research should be carried out with consideration to other aspects of corporate governance other than the ones considered for the study with a view of finding out if the study findings will be consistent with the current study. This is because the principles of corporate governance are numerous and the study considered only four. In addition, instead of using a survey, other methods of data collection i.e. interviews may provide different results. It is expected that two-way communication via an interview could
produce other meaningful results; however, non-anonymous methods such as interviews can be problematic in revealing the truth, especially when questioning respondents regarding governance matters, as failure to appropriately address the questions would harm or embarrass respondents.

Further study should also be undertaken on corporate governance legislation reforms as an environmental base for strategic position taken to generate funds, and at the same time manipulate social as well as political demands of the nation.

Moreover, further studies should be done on the challenges of corporate governance and the effect of these challenges on the financial performance of the saccos. The same study should be carried out in other sectors such as manufacturing and processing firms to find if the same results will be obtained.

Finally, it would be more rewarding if further studies on corporate governance were to take on a more holistic approach to performance. This should include operational efficiency and other non-financial performance indicators.
REFERENCES


Appendix 1: Data Collection Form

A. SACCO PROFILE

1. Name of the Sacco……………………………………………………………………

2. Year of Establishment………………………………………………………………

3. Current Number of employees (Tick where appropriate)

   Below 20 { } 21-50 { } 51-100 { } 101 and above { }

B. FINANCIAL PERFORMANCE OF THE SACCO OVER THE LAST 5 YEARS.

<table>
<thead>
<tr>
<th>Year/ Performance measure</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
<th>2012</th>
<th>2013</th>
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<tbody>
<tr>
<td>NET INCOME (Total Revenue – Total expenses)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total Assets (Current + Non-current Assets)</td>
<td></td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>ROA (Net income / Total Assets)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>Total Debt (Short term + Long term liabilities)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Equity – Share Capital</td>
<td></td>
<td></td>
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</tr>
</tbody>
</table>
C. CORPORATE GOVERNANCE MEASURES

<table>
<thead>
<tr>
<th>Year</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
<th>2012</th>
<th>2013</th>
</tr>
</thead>
<tbody>
<tr>
<td>A. Board Size- What is the number of the board of directors</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>B. No of board meetings</td>
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<td></td>
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<td></td>
<td></td>
</tr>
<tr>
<td>C. Gender Diversity- What is the women composition in your board</td>
<td></td>
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<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>D. Average age of all directors</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>E. Board ownership – Totals shares held by the board / Total shares of all members</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>F. Average compensation of the board</td>
<td></td>
<td></td>
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<td></td>
<td></td>
</tr>
</tbody>
</table>
Appendix 2: Deposit Taking Saccos Regulated by SASRA in 2013

1. AFYA SACCO SOCIETY LTD
2. AIRPORTS SACCO SOCIETY LTD
3. ASILI SACCO LTD
4. BANDARI SACCO SOCIETY LTD
5. BARAKA SACCO SOCIETY LTD
6. BARI NGO SACCO SOCIETY LTD
7. BIASHARA SACCO SOCIETY LTD
8. BINGWA SACCO SOCIETY LTD
9. BORABU SACCO SOCIETY LTD
10. BORESHA SACCO SOCIETY LTD
11. BUNGOMA TEACHERS SACCO SOCIETY LTD
12. BURETI SACCO SOCIETY LTD
13. BUSIA TESO TEACHERS SACCO SOCIETY LTD
14. CAPITAL SACCO SOCIETY LTD
15. CENTENARY SACCO SOCIETY LTD
16. CHAI SACCO SOCIETY LTD
17. CHEMELIL SACCO SOCIETY LTD
18. CHEPSOL SACCO SOCIETY LTD
19. CHUNA SACCO SOCIETY LTD
20. COMOCO SACCO SOCIETY LTD
21. COSMOPOLITAN SACCO SOCIETY LTD
22. COUNTY SACCO SOCIETY LTD
23. DAIMA SACCO SOCIETY LTD
24. DHABITI SACCO SOCIETY LTD
25. DIMKES SACCO SOCIETY LTD
26. EGERTON SACCO SOCIETY LTD
27. EMBU TEACHERS SACCO SOCIETY LTD
28. ENEA SACCO SOCIETY LTD
29. FARIJI SACCO SOCIETY LTD
30. FORTUNE SACCO SOCIETY LTD
31. FUNDILIMA SACCO SOCIETY LTD
32. GITHUNGURI DAIRY & COMMUNITY SACCO SOCIETY LTD
33. GUSII MWALIMU SACCO SOCIETY LTD
34. HARAMBEE SACCO SOCIETY LTD
35. HAZINA SACCO SOCIETY LTD
36. IMENTI SACCO SOCIETY LTD
37. IRIANYI TEA SACCO SOCIETY LTD
38. ISIOLO TEACHERS SACCO SOCIETY LTD
39. JAMII SACCO SOCIETY LTD
40. JIJENGE SACCO SOCIETY LTD
41. KAKAMEGA TEACHERS SACCO SOCIETY LTD
42. KEIYO TEACHERS SACCO SOCIETY LTD
43. KENPIPE SACCO SOCIETY LTD
44. KENVERSITY SACCO SOCIETY LTD
45. KENYA BAKERS SACCO SOCIETY LTD
46. KENYA CANNERS SACCO SOCIETY LTD
47. KENYA HIGHLANDS SACCO SOCIETY LTD
48. KENYA MIDLAND SACCO SOCIETY LTD
49. KENYA POLICE STAFF SACCO SOCIETY LTD
50. KIAMBAADDAIRY RURAL SACCO SOCIETY LTD
51. KILIFI TEACHERS SACCO SOCIETY LTD
52. KINGDOM SACCO SOCIETY LTD
53. KIPSIGIS EDIS SACCO SOCIETY LTD
54. KIPSIGIS TEACHERS SACCO SOCIETY LTD
55. KITE SACCO SOCIETY LTD
56. KITUI TEACHERS SACCO SOCIETY LTD
57. KMFRI SACCO SOCIETY LTD
58. KONOIN SACCO SOCIETY LTD
59. K-UNITY SACCO SOCIETY LTD
60. KURIA TEACHERS SACCO SOCIETY LTD
61. LAIKIPIA TEACHERS SACCO SOCIETY LTD
62. LENGO SACCO SOCIETY LTD
63. MAGADI SACCO SOCIETY LTD
64. MAGEREZA SACCO SOCIETY LTD
65. MAISHA BORA SACCO SOCIETY LTD
66. MARAKWET TEACHERS SACCO SOCIETY LTD
67. MARSABIT TEACHERS SACCO SOCIETY LTD
68. MENTOR SACCO SOCIETY LTD

60
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<th>NAME OF SOCIETY</th>
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<td>METROPOLITAN TEACHERS SACCO SOCIETY LTD</td>
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<td>MMH SACCO SOCIETY LTD</td>
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<td>MOMBASA TEACHERS SACCO SOCIETY LTD</td>
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<td>MUMIAS OUTGROWERS SACCO SOCIETY LTD</td>
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<td>NACICIO SACCO SOCIETY LTD</td>
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<tr>
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<td>NAKU SACCO SOCIETY LTD</td>
</tr>
<tr>
<td>82</td>
<td>NAME OF SOCIETY</td>
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<td>NYAMBENE ARIMI SACCO SOCIETY LTD</td>
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</table>
92. NYAMIRA TEA FARMERS SACCO SOCIETY LTD
93. NYERI TEACHERS SACCO SOCIETY LTD
94. ORTHODOX DEVELOPMENT SACCO SOCIETY LTD
95. SAFARICOM SACCO SOCIETY LTD
96. SAMBURU TRADERS SACCO SOCIETY LTD
97. SHERIA SACCO SOCIETY LTD
98. SIAYA TEACHERS SACCO SOCIETY LTD
99. SIMBA CHAI SACCO SOCIETY LTD
100. SIRAJI SACCO SOCIETY LTD
101. SOLUTION SACCO SOCIETY LTD
102. SOT TEA GROWERS SACCO SOCIETY LTD
103. SOTICO SACCO SOCIETY LTD
104. STIMA SACCO SOCIETY LTD
105. SUKARI SACCO SOCIETY LTD
106. TAI SACCO SOCIETY LTD
107. TAIFA SACCO SOCIETY LTD
108. TAITA TAVETA TEACHERS SACCO SOCIETY LTD
109. TEMBO SACCO SOCIETY LTD
110. TENHOS SACCO SOCIETY LTD
111. THAMANI SACCO SOCIETY LTD
112. THARAKA NITHI TEACHERS SACCO SOCIETY LTD
113. THIKA DISTRICT TEACHERS SACCO SOCIETY LTD
114. TIMES U SACCO SOCIETY LTD
115. TOWER SACCO SOCIETY LTD
116. TRANS NZOIA TEACHERS SACCO SOCIETY LTD
117. UKRISTO NA UFANISI WA ANGLICANA SACCO SOCIETY
118. UKULIMA SACCO SOCIETY LTD
119. UNAITAS SACCO SOCIETY LTD
120. UNITED NATIONS SACCO SOCIETY LTD
121. UNIVERSAL TRADERS SACCO SOCIETY LTD
122. WAKENYA PAMOJA SACCO SOCIETY LTD
123. WAKULIMA COMMERCIAL SACCO SOCIETY LTD
124. WANAANGA SACCO SOCIETY LTD
125. WANANCHI SACCO SOCIETY LTD
126. WANANDEGE SACCO SOCIETY LTD
127. WARENG SACCO SOCIETY LTD
128. WASHA SACCO SOCIETY LTD
129. WAUMINI SACCO SOCIETY LTD
130. YETU SACCO SOCIETY LTD

SOURCE: SASRA WEBSITE, www.sasra.go.ke
Appendix 4: Introduction Letter - UON

UNIVERSITY OF NAIROBI
SCHOOL OF BUSINESS
MBA PROGRAMME

DATE 23/07/2013

TO WHOM IT MAY CONCERN

The bearer of this letter: JAMES NYAGA KAMAU
Registration No: D61/60913/2013

Is a bona fide continuing student in the Master of Business Administration (MBA) degree program in this University.

He/ She is required to submit as part of his/her coursework assessment a research project Report on a management problem. We would like the students to do their projects on real problems affecting firms in Kenya. We would, therefore, appreciate your assistance to enable him/her collect data in your organization.

The results of the report will be used solely for academic purposes and a copy of the same will be availed to the interviewed organizations on request.

Thank you.

PATRICK NYABUTO
MBA ADMINISTRATOR
SCHOOL OF BUSINESS
Appendix 5: Data Collection Request Letter to SASRA

JAMES NYAGA KAMAU,
P. O. BOX 55322-00200,
NAIROBI.
jakany2@gmail.com.com

30th JULY 2014,

THE CHIEF EXECUTIVE OFFICER,
SASRA,
NAIROBI.

Dear Sir,

REF: REQUEST FOR RESEARCH DATA ON DEPOSIT TAKING SACCOs WITHIN NAIROBI – MBA FINANCE UNIVERSITY OF NAIROBI

The above subject matter refers.

I am a student from the University of Nairobi, pursuing an MBA in Finance. One of the requirements for the degree award is to undertake an academic research. Due to my great interest in the co-operative movement I choose to undertake a study on “THE EFFECT OF CORPORATE GOVERNANCE ON THE FINANCIAL PERFORMANCE OF SACCOS REGULATED BY SASRA”.

To enable me undertake the same I am kindly requesting for information on 24 Saccos (See attached list) located within Nairobi as per the attached data collection form, also attached is an introductory letter from the University of Nairobi.

The information so received will be treated in confidence and will solely be used for academic purposes only.

I will highly appreciate your kind assistance. Meanwhile, thank you in advance.

Kind Regards,

James Kamau