DECLARATION

This Research Project is my original work and has not been submitted for examination in any other university or college for examination/academic purposes.

Signed: ……………………………………… Date: ………………………………………

ANTHONY ABIRA
Reg. No.: D61/79196/2012

This Research Project has been submitted for examination with my approval as the university supervisor.

Signed: ……………………………………… Date: ………………………………………

Name: MR. HERICK ONDIGO
Department of Finance & Accounting
School of Business
University of Nairobi
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DEDICATION

I dedicate this study to my dear family members and friends for all the support they gave me all the time as I prepared and worked on this project.
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LIST OF ABBREVIATIONS

ANOVA: Analysis of variance
CEO : Chief executive Officer
ISDA : International Swaps and Derivatives Association
NSE : Nairobi Securities Exchange
ROA : Return on Assets
ROE : Return on Equity
SPSS : Statistical Package for Social Sciences
ABSTRACT

This study investigates the effect of ownership structures on financial performance of companies listed in the NSE. In particular, the study seeks to enhance understanding on the issue by finding out how the financial performance is affected by the ownership structures. The study is conducted based on a sample of sixty two companies listed on the Nairobi Securities Exchange during the period 2008-2013. Ownership structure relates to the decision making segment of the firm. The term ‘ownership structure’ has two widely applied dimensions: ownership concentration and owner identity. Ownership concentration measures the degree of concentration of voting rights. The voting rights of the largest shareholder and the sum of voting rights of the second and third largest shareholder measures it. Ownership identity was further broken down into foreign ownership, institutional ownership, Government ownership and diverse ownership. The empirical analysis on the effects of ownership structure on financial performance is conducted on the whole population of the companies listed in the Nairobi Securities Exchange. Empirical analysis is conducted using the linear regression analysis method. The Study found out the financial performance of Kenyan firms can best be explained the ownership concentration and ownership identity. The study found a positive relationship between ownership concentration and financial performance. A positive relationship between financial performance and ownership identity was also observed. These results have important implications on policy and therefore provides a number of policy recommendations, such as showing a need to reasonably diversify shareholding as a way of attracting more skills and competencies among the shareholders that can be tapped to improve firm performance.
CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

Business organisations are created with the sole purpose of making returns that depends on their decision-making mechanisms. Organization decisions also affect its capital base and the plans of either going for equity financing or debt financing. In debt financing, companies borrow money or capital and resources from external sources that are to be repaid over a period, usually with interest (Raji, 2012). The stock markets are widely regarded as central for the functioning of modern capitalist economies. There has been a great paradigm shift in the corporate governance arena as more and more organizations integrate the ownership structure ideology into their operations.

The separation of ownership and control in Modern Corporation introduced by Berle and Means (1932) retains a central position in the economic theory of the firm. They claim that “the separation of ownership from control produces a condition where the interest of owner and ultimate manager may, and often do, diverge, and where many checks that formerly operated to limit the use of power disappear.” Every firm has several ways of building its ownership. Normally the type of ownership structure a firm decides to adopt is engineered by the vision of the company. According to Kumar (2003), corporate governance is an important effort to ensure accountability and responsibility and a set of principles, which should be incorporated into every part of the organization.

The ownership structure is defined by the distribution of equity with regard to votes and capital as well as the identity of the equity owners. These structures are of major importance in corporate governance because they determine the incentives of managers and thereby the economic efficiency of the corporations they manage (Jensen and Meckling, 1976). The corporate governance framework according to Imam and Malik (2007) is the widest control mechanism (both internal and external) since it encourages the efficient use of corporate resources and ensures accountability for the stewardship of those resources utilised. Lins (2002) further contend that corporate governance could help to align the interests of individuals, corporations and society through a fundamental ethical basis and it will fulfil the long-term
strategic goal of the owners, building shareholder value and establishing a dominant market share.

According to Ezazi, et al. (2011), ownership can also be formed through capitalization, which can be obtained through retained earnings, loans from banks, venture capital or going public. Each of these possibilities has its own advantages and disadvantages. In finance, capital structure refers to the way a corporation finances its assets through some combination of equity, debt, or hybrid securities (Raji, 2012). A firm’s capital structure is then the composition or ‘structure’ of its liabilities and assets. The capital structure of a firm is actually a specific mixture of debt and equity a firm employs in financing its operation (Gorton & Schmid, 1996). Other factors identified by Ezazi, et al., (2011) with regard to firms ownership structure included volatility in earnings, asset tangibility, dividend payout ratio and profitability are determinants of corporate capital structure decisions within trading firms.

More equity ownership by the manager may increase corporate performance because it means better alignment of the monetary incentives between the manager and other equity owners (Jensen and Meckling, 1999). More equity ownership by the manager may increase corporate performance because the managers are more capable of opposing a takeover threat from the market for corporate control and as a result, the raiders in this market will have to pay higher takeover premiums (Ezazi, et al., 2011). On the other hand, Fama and Jensen (2000) content that increased ownership concentration (any kind of owner) decreases financial performance because it raises the firm's cost of capital as a result of decreased market liquidity or decreased diversification opportunities on behalf of the investor.

Berle and Means as early in 1932 pointed out the fundamental principal-agent conflict. Firms had transformed themselves from privately owned and entrepreneurial driven entities into public companies, to reap the benefits of scale and scope available in the domestic market of the time (Chandler, 1990). Over the last twenty years, the world has also witnessed fundamental changes in how ownership is organised. Large-scale privatisation programmes significantly reduced government control and moved enterprises into the private sector, and previous privately controlled firms raised equity capital on public markets.
1.1.1 Ownership Structure

Ownership structure relates to the decision making segment of the firm. The term ‘ownership structure’ has two widely applied dimensions: ownership concentration and owner identity. Zhuang (1999) argue that ownership structure is one of the most important factors in shaping the corporate governance system of any country. This is because it determines the nature of the agency problem. That is, whether the dominant conflict is between managers and shareholders, or between controlling and minority shareholders. Zhuang identified two important aspects of corporate ownership structure as concentration and composition. He observes that the degree of ownership concentration in a firm determines how power is distributed between its shareholders and managers. When ownership is dispersed, shareholding control tends to be weak because of poor shareholder monitoring the author affirms. For instance, a small shareholder is unlikely to be interested in monitoring because he/she would bear all the costs of monitoring hence share a small proportion of the benefits (Zhuang, 1999). This raises the question, what if all small shareholders behave this way. Then no monitoring of managerial efforts would take place. Zhuang further argues that when ownership of a company is concentrated, large shareholders would play an important role to monitor the management. However, he says that the only problem with this form of ownership is how minority shareholders would be protected from exploitation by controlling shareholders who may act in their own interests at their expense. Secondly, ownership composition tries to define who the shareholders are and who among them belongs to the controlling groups.

It can be assumed that better overlap between ownership and control should indeed lead to a reduction in conflicts of interest therefore higher firm value (Holderness, 2009). He further states that it can be complicated when looking at how ownership, control and firm value are related. For example, management owning a company can serve to better put in line managers’ interests with those of the shareholders of the company. On the other hand, if managers and shareholders’ interests are not completely aligned, higher stake in the company can give managers greater freedom to pursue their own goals without fear of reprisal. Hence, the effect of managerial ownership on the value of the firm depends on the trade-off between the alignment and entrenchment effects (Denis & McConnell, 2002). Furthermore, the divergence of voting right and capital right allow shareholders to gain control with little equity involvement through mechanisms such as dual class equity, pyramiding, etc. Thus, divergence should be taken into
consideration when analyzing the effect of ownership structure on firm performance. Ownership concentration measures the degree of concentration of voting rights. The voting rights of the largest shareholder and the sum of voting rights of the second and third largest shareholder measures it. Furthermore, the divergence ratio of the largest shareholder illustrates ownership concentration from another perspective. Owner identity is based on the type of the largest shareholder.

1.1.2 Firm Performance
Performance is the outcome of all of the organisation's operations and strategies (Wheelen and Hunger, 2002). Measuring performance accurately is critical for accounting purposes and remains a central concern for most organisations. Performance measurement systems provide the foundation to develop strategic plans, assess an organisation's completion of objectives, and remunerate managers (Ittner and Larcker, 1998).

Although assessment of performance in the past literature is still very important, it is also complicated (Pont and Shaw, 2003). While consensual measurement of performance promotes scholarly investigations and can clarify managerial decisions, managers have not been able to find clear, current and reliable measures of performance on which marketing merit could be judged. Two approaches have been adopted in the literature to measure financial performance. The first subjectively measures the performance of firms based on their own evaluation and expectations or comparison with their competitors. The second is objective, based on the absolute measure of performance such as financial ratios (Appiah-Adu, 1998). The aim of this thesis is to examine whether firm performance is affected by ownership structure. The study will be looking at the financial performance and therefore will consider the profitability side of firm performance indicated by return on equity (ROE).

1.1.3 Ownership Structure and Firm Performance
The influence of ownership structures on firm performance has been researched extensively in the theoretical and empirical literature. The relevant literature suggests that ownership structure is one of the main corporate governance mechanisms influencing the scope of a firm’s agency cost. Jensen and Meckling (1976) suggested that ownership concentration has a positive effect on performance because it alleviates the conflict of interest between owners and managers.
Ownership structure, as a mechanism in corporate governance to facilitate increased efficiency of a firm, has been believed to affect firm performance for many years.

1.1.4 Firms Listed at the Nairobi Securities Exchange

The NSE is the principal stock exchange of Kenya. It was constituted as Nairobi Stock Exchange in 1954 as an overseas stock exchange while Kenya was still a British colony with permission of the London stock exchange (NSE, 2014). In July 2011, the Nairobi Stock Exchange Limited changed its name to the Nairobi Securities Exchange Limited. The change of name reflected the strategic plan of the Nairobi Securities Exchange to evolve into a full service securities exchange which supports trading, clearing and settlement of equities, debt, derivatives and other associated instruments.

The NSE had 62 listed companies as at September 4th 2014 and is considered one of the largest stock markets in Africa (KenInvest, 2014). It is, through the NSE, that many Kenyan entities are able to raise capital and expand their business activities. Since 1990, Kenyan companies have raised around $1 billion through initial public offerings. The expansion of these companies is really boosting the Kenyan economy. The study therefore considers the NSE to be a good representative population to study because companies listed herein consists of many sectors of the Kenyan economy as well as the diversity in ownership structures.

1.2 Research Problem

The influence of ownership structures on firm performance has been researched extensively in the theoretical and empirical literature. This might be due to the fact that this is the decision making segment of a firm, which makes ownership powers influential in firm decisions. The relevant literature suggests that ownership structure is one of the main corporate governance mechanisms influencing the scope of a firm’s agency cost. The main objective of a firm being to maximize profits, the profitability of a firm, which highly relies on decisions made in the firm by the business owners, is bound to affect the firm’s financial performance.

The case for ownership structure for the firms trading in the stock market is quite complex and hard to grasp given that the company is always changing ownership from one majority shareholder to another. This case is complicated by the fact that as long as the company’s shares are trading, their ownership is bound to change at any time. The Nairobi Securities Exchange is
one quite busy hub in East Africa where companies change hands by a click of the mouse. Many companies have changed hands from government ownership to private ownership or to public ownership through this market. Therefore, most of the companies trading in the Nairobi Securities Exchange are not entirely private, government or public owned, hence their ownership structure cannot be easily defined, though most consider ownership by the majority shareholder. The different majority shareholders over time are bound to have made some impact on the firm performance, a phenomenon the study desires to set straight.

The ownership structure of firms has been a very exciting area by scholars who have widely contributed on the topic. However, the relationship between ownership structure and firm performance is complex and empirical studies done on the area have proved so (Demsetz, 1983, Demsetz and Lehn 1985; Shleifer and Vishny 1986; Wu and Cui 2002; Cornett et al. 2007; Alam et al. 2008; Ezazi, et al. 2011; Mang’unyi 2011; Warrad et al. 2013;). The effect of ownership structures on the corporate performance has shown contradicting conclusions from former studies. While Shleifer and Vishny (1986), Berle and Means (2002), Cortnett (2007) and Alam et al. (2008) found positive effect of high concentration on firm performance; Demsetz (1983), Demsetz and Lehn (1985),Demsetz (2001)and Ezazi (2011) found the effect to be negative. Furthermore, studies related to owner identities and firm performance also have contradicting conclusions. illustrate with managerial ownership, when Jensen (1990),Cortnett (2007), Holderness, (2009) found positive effect of managerial ownership on firm performance; Mang’unyi(2011) and Warrad et al. (2013) found the effect to be negative and argued the existence of managerial entrenchment.Since these results are conflicting and ambiguous, it becomes interesting to study the nature of this relation in the case of public trading corporations, which present differences in terms of political, economic and institutional conditions.

On top of the conflicting viewpoint, there has been very little interest on the ownership structures of the firm within the Kenyan front. The only study in Kenya accessible was done by Mang’unyi (2011) and concentrated on the impact of ownership structure on corporate governance than on performance of the firm. This study hopes to fill this research gap by looking at the effect of ownership structure on financial performance on companies listed on Nairobi Securities Exchange (NSE). Stock markets are widely viewed as important, if not essential, for the functioning of modern capitalist economies. The NSE is one of the best performing stocks
exchange firms. The study intends to address the question: what is the effect of ownership structure on financial performance of companies listed in the NSE?

1.3 Objective of the Study
To determine the effect of ownership structures on financial performance of companies listed in the NSE.

1.4 Value of the Study
This study hopes to enhance understanding on the issue by finding out how the financial performance is affected by the ownership structures. The study will be beneficial to the companies involved in the study since the findings of this study will provide new knowledge useful in enhancing the knowhow on pros and cons on institutional ownership and the likely outcomes of such structures. The firm management will benefit from the study as they will acquire information that directly relates to their decision-making paradigm and be able to carry out their day-to-day operations. The findings of this study will also add new information to the existing body of literature on ownership structure that can be referenced to in future, therefore benefitting scholars and researchers.
CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction
This chapter contains the literature review of the study. The chapter discusses the theoretical review that covers theories related to ownership structures such as the agency theory, stakeholder theory and stewardship theory. There is a theoretical look at the relationship between ownership structure and firm performance with identity and concentration view taking centre stage. An empirical review on the success of the study concept followed by a summary of literature review culminates the chapter for the study.

2.2 Theoretical Review
This section reviews some of the ownership structure theories with a view to understand how they relate to firm performance. Several theories exist that attempt to highlight the firm ownership and how the firm’s performance is affected by these structures when meeting its obligations. The study considered three key theories that inform the study that includes agency theory, stakeholder theory and stewardship theory.

2.2.1 Agency Theory
The first detailed description of agency theory was presented by Jensen and Meckling in 1976 (Abdullah & Valentine, 2009). In Agency theory, shareholders who are the owners or principals of the company, hires the agents to perform work. Principals delegate the running of business to the directors or managers, who are the shareholder’s agents (Clarke, 2004). In the agency theory, shareholders expect the agents to act and make decisions in the principal’s interest. On the contrary, the agent may not necessarily make decisions in the best interests of the principals. Such a problem was first highlighted by Adam Smith in the 18th century and subsequently explored by Ross. The agent may succumbed to “self-interest, opportunistic behaviour and falling short of congruence between the aspirations of the principal and the agent’s pursuits” (Abdullah et al., 2009). Given that the managers may not act to maximize the returns to shareholders, it follows therefore, that the appropriate governance structures need to be implemented to safeguard the interests of shareholders. The board of directors is therefore
constituted to ameliorate the risk or cost of agency (Finegold et al. (2007). The appointment of outside directors is to ensure objectivity to other internal directors’ decisions.

Agency theory identifies the relationship where one party, the principle, delegates work to another, the agent (Mallin, 2010). The principal-agent model regards the central problem of corporate governance as self-interested managerial behaviour in a universal principal-agent relationship. Agency problems arise when the agent does not share the principal's objectives. Furthermore, the separation of ownership and control increases the power of professional managers and leaves them free to pursue their own aims and serve their own interests at the expense of shareholders (Berle and Means, 1932).

This separation is however, linked and governed through proper ‘agency relationship’ at various levels, among others ‘between shareholders and boards of directors, between boards and senior management, between senior and subordinate levels of management’ (Hayes and Abernathy, 1980). In such a principal-agent relationship, there is always ‘inherent potential for conflicts within a firm because the economic incentives faced by the agents are often different from those faced by the principals. According to International Swaps and Derivatives Association (ISDA 2002), all companies are exposed to agency problems, and to some extent develop action plans to deal with them.

### 2.2.2 Stakeholders’ Theory

The Stakeholder theory was embedded in the management discipline in 1970 and was gradually developed by Freeman in 1984 incorporating corporate accountability to a broad range of stakeholders (Abdullah et al. 2009). Wheeler, Colbert, & Freeman (2003) argued that stakeholder theory 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, ethics, political theory, economics, law and organizational science. Stakeholder theorists suggest that managers in organizations have a network of relationships to serve. This network includes the suppliers, employees, business partners, customers and the community and it is argued that this group of network is more important than the owner-manager-employee relationship in agency theory (Addullah & Valentine, 2009). Stakeholder theorists suggest that the firm is a system, where there are stakeholders and the purpose of the organization is to create wealth for its stakeholders. The theory posits that the boards of directors
for corporations should be constituted in such a manner that all the stakeholders are taken care of. In many countries therefore, especially in Europe and Asia, stakeholder models of governance, which emphasize the board’s role in representing employee and community interests as well as those of owners, are common, (Yoshimor, 2005).

There are two main theories of stakeholder governance: the abuse of executive power model and the stakeholder model. Current corporate governance arrangements vest excessive power in the hands of management who may abuse it to serve their own interest at the expense of shareholders and society as a whole (Hutton, 1995). Supporters of such a view argue that the current institutional restraints on managerial behaviour, such as non-executive directors, the audit process, the threat of takeover, are simply inadequate to prevent managers abusing corporate power. Shareholders protected by liquid asset markets are uninterested in all but the most substantial of abuses. Perhaps the most fundamental challenge to the orthodoxy is the stakeholder model, with its central proposition, with a wider objective function of the firm is more equitable and more socially efficient than one confined to shareholder wealth.

2.2.3 Stewardship Theory

Davis et al. (1997) developed the stewardship theory of management as a counter strategy to agency theory. Stewardship theory of management and agency theory have both focused on the leadership philosophies adopted by the owners of an organization. It grew out of the seminal work by Donaldson and Davis (1989, 1991) and was developed as a model where senior executives act as stewards for the organization and in the best interests of the principals. The model of man in stewardship theory is based upon the assumption that the manager will make decisions in the best interest of the organization, putting collectivist options above self-servicing options. This type of person is motivated by doing what is right for the organization, because she believes that she will ultimately benefit when the organization thrives. The steward manager maximizes the performance of the organization, working under the premise that both the steward and the principal benefit from a strong organization (Mallin, 2010).

Stewardship theory has its roots from psychology and sociology and was illustrated by Davis, Schoorman, & Donaldson (1997) thus: “...as a steward protects and maximizes shareholders wealth through firm performance, because by so doing, the steward’s utility functions are maximized” (Abdullah & Valentine, 2009). The stewardship perspective suggests that stewards
are satisfied and motivated when organizational success is attained. Stewardship theory recognizes the importance of structures that empower the steward and offers maximum autonomy built on trust. It stresses on the position of employees or executives to act more autonomously so that the shareholders’ returns are maximized. In this sense, it is believed that the firm’s performance can directly affect perceptions of their individual performance. Stewardship theory suggests unifying the role of the CEO and the chairman so as to reduce agency costs and to have greater role as stewards in the organization.

The stewardship theory suggests that managers will be self-motivated to act in the best interest of the shareholders and therefore, when appropriately empowered would give better returns to the shareholders without any need for monitoring or further incentives. To this end therefore, the theory posits that more inside directors would yield better returns to the shareholders. While the theory has acquired a lot of credence in light of the recent research findings, it fails, however, to provide solutions to the increasing corporate scandals across the world, which seems to suggest a need for increased management monitoring.

2.3 Determinants of Firm Performance
A large number of previous studies relating to firm’s performance or sometimes corporate performance has identified a number of factors that empirically and even significantly affecting the firm’s performance. Zeitun and Tian (2007) with the extension in their regression model by adding liquidity and non-debt tax shield and applied this regression model simultaneously on and food sectors of Pakistan. The findings of Zeitun and Tian (2007) indicated that leverage has a significant and negative relationship with firm’s performance. They used leverage, growth, size, tax, risk and tangibility as independent variable to see their effect on firm’s performance. They concluded that firm’s size and tax have positive and significant relationship with firm’s performance while risk and tangibility have negative and significant relationship with firm’s performance. Memon, Bhutto and Abbas (2010) concluded in their study of capital structure and firm’s performance on textile sector that the companies in this sector are performance below optimum level of capital structure and also fail to achieve the economies of scale. Nosa and Ose (2010) found that effective funding required for the growth and development of the corporations in Nigeria. They suggested enhancing the regulatory framework for increasing the firm’s performance by focusing on risk management and corporate governance. Onaolapo and Kajola
(2010) found a significant and negative relationship between debt ratio and firm’s financial performance. The study conducted by Krishnan and Moyer (1997) found a negative and significant relationship between leverage and firm’s performance while other factors affecting firm’s performance positively includes size, growth, tax and risk. Jensen and Meckling (1976) found two types of agency cost; agency cost of equity holders and agency cost of debt holders. They concluded that a conflict of interest arises between the management and the shareholders when management take decision against the interest of shareholders and another conflict arises when the shareholder act against the interest of debt holders. William (1987) found that decision for high leverage by the management decreases the conflict between management and shareholders. The leverage can work as disciplinary device that controls the management from wasting their firm’s resources. The researcher in the current study used short term as well as long term debts as proxy for leverage and also the other factors like ownership structure, ownership concentration, ownership identity and firm size for measuring how they determine firm’s performance.

2.3.1 Ownership structure
Firm performance is supposed to be independent from the ownership structure in the absence of agency cost. However, in the real world, the agency cost generated from principal-agent problems exists widely. Equity ownership structure as an important mechanism in corporate governance (Denis & McConnell 2003), influence the quality of corporate governance and its ability to reduce agency costs (Berk & DeMarzo, 2007). The path dependent argument (Dyck 2004) state that the ownership structures are path dependent, and are determined by the stakes. Therefore, the current ownership structure may not be the most efficient one. Thus, testing the relationship between ownership structure and financial performance could help the investors to gain value by optimizing the firm’s ownership structure.

The effect of ownership structure on firm performance may be looked at according to two dimensions, ownership concentration and owner identities. Ownership concentration provides quantitative information about the capital right of the largest shareholder(s). Owner identity information provides qualitative information about the character of the controlling shareholder(s). One issue to pay attention to is the divergence of capital right and voting (control) right. Normally the two kinds of right are the same, however, when the voting right is
different from the capital right due to control mechanisms, the incentives of the principals and agents would get influenced, (Gross, 2007).

Various forms of ownership structure exist that affects performance. In Kenya, key reforms have encouraged foreign companies to venture into the Kenyan market. Kamau (2009) affirm that foreign banks are more efficient than local banks. She attributes this to the fact that foreign banks concentrate mainly in major towns and target corporate customers, whereas large local banks spread their activities more widely across the country. Foreign banks therefore refrain from retail banking to specialise in corporate products, while large domestic banks are less discriminatory in their business strategy. These different operational modalities affect efficiency and profitability she affirms, which is dependent on the institutional owners decisions.

2.3.2 Ownership Concentration
The first attempt to study the effect of ownership concentration on company profitability was done by Berle and Means (1932). Since then there has been several studies and according to Cubbin and Leech (1983) the share of the largest owner often categorizes such studies comparing profitability of manager–and owner–controlled companies. Findings of these studies usually showed a higher rate of return in companies with concentrated ownership (Cubbin and Leech, 1983) but lacked a theoretical foundation. They neither used nor provided a theory of ownership structure and seemed to imply that shareholders could profit by rearranging their portfolios. Theoretically, the ownership structure of the firm is an endogenous outcome of the competitive selection in which various cost advantages and disadvantages are balanced to arrive at an equilibrium organization of the firm (Demsetz & Villanonga, 2001).

Some studies investigate the effect of ownership concentration on growth and risk. For example, Hu, et al. (2008), use the variance in profit/equity ratio as an expression of risk and tested its dependence on the ownership concentration using a sample of 187 of the largest 500 Japanese non-financial firms. The study found that there is an insignificant positive relationship between manager-controlled firms (as opposed to owner-controlled) and a high variance in profit/equity. In other words low ownership concentration may imply higher risk. The main explanation of the positive effect is that block holders has both the ability and the incentive to monitor and control agents, in order to operate the firm for the good of the shareholders. This is defined as incentive alignment. The cost-efficiency of monitoring by block holders yields a better performance of the
firm. However, in the cases where there is a large divergence of control right and cash flow right, block holder has less incentive to monitor the managers to pursue profit-maximization goal. Other studies, which find negative effects, argue that the increased control by block holders reduces the self-realization of managers who consequently get discouraged. This phenomenon is defined as over-monitoring (Brown & Caylor, 2006).

### 2.3.3 Ownership Identity

A significant amount of literature on firm performance has paid much attention to the issue of shareholder identity (Shleifer and Vishny, 1997; Kumar, 2003; and Raji, 2012). Most sampled literature indicates that the objective functions and the costs of exercising control over managers vary substantially for different types of owners. This implies that, it is not only important to know how much equity a shareholder owns, but rather who this shareholder is. The reason for this is that investors differ in terms of wealth, risk aversion and the priority they attach to shareholder value relative to other goals. This is because shareholder interests influence owner preferences and investment choices, (Kibuthu, 2005). Additionally, conflicts of interest may arise since owners have their economic relations with the firm. For instance, a bank may play a dual role as lenders and owners, government as regulators and owners (Clarke, 2004). For each of these stakeholders, preferences regarding company strategy will involve a trade-off between the pursuit of shareholder value and other goals. Ezazi, (2011) posited that firm performance is positively related to the majority shareholder. This single shareholder controls more than half of a corporation’s shares, or sometimes, one of a small group of shareholders who collectively control more than half of a corporation’s outstanding shares. Imam & Mahfuja, (2007) indicated that a majority shareholder has a negative influence on firm performance. Their reasons were that firms having single ultimate owner operate under strong ownership and therefore experience higher productivity growth. This effect is clearer under stronger product market competition. Competition leads to a positive effect, which affect productivity growth rate by majority shareholder.

Managerial ownership seems to be the most controversial ownership form as it has ambivalent effects on firm performance and is considered a tool for alignment of managerial interests with those of shareholders, and at the same time promotes entrenchment of managers. The latter is especially costly when they do not act in the interest of shareholders (Abdullah & valentine,
2009; Charfeddine & Elmarzougui, 2010). Thomsen and Pedersen (2000) posit that the relationship between ownership concentration (as a proxy for shareholder control over managers) and firm performance depends on the identity of the large (controlling) shareholders. The general impact of managerial ownership on corporate performance depends on the relative strengths of the incentive alignment and entrenchment effects.

State ownership on the other hand has been regarded as inefficient and bureaucratic. Vickers and Yarrow (1988) consider the lack of incentives as the major argument against state ownership. Ngoc (2007) indicated that price policy whilst Shleifer and Vishny (1994) stated political intervention and human capital problems as some of the challenges state ownership structure influences performance. Notwithstanding these challenges, state ownership of firms is not without some benefits to the society. Public enterprises help cure market failures and state control seems to be more economically desirable as a way of restoring the purchasing power of the citizenry (Mang’unyi 2011). Aside these benefit state firms have been empirically seen to be highly inefficient and performed poorly as compared to private ones even in pursuing public interests (Gross, 2007).

The effect of foreign ownership on firm performance has been an issue of interest to both academics and policy makers. As posited by Ngoc (2007), the main challenging question in the international business strategy is the outcome gained from foreign ownership of firms. It is duly accepted that foreign ownership plays a crucial role in firm performance, particularly in developing and transitional economies, researchers such as Thomsen & Pedersen (2000), have concluded that, on average, multi-national enterprises have performed better than the domestically owned firms have. It is therefore, not surprising that the last two decades have witnessed increased levels of foreign direct investments in the developing economies.

2.3.4 Firm size

The nature of the relationship between firm size and economic performance has received considerable attention in the literature and has provoked vigorous debate. Several arguments favour larger firm sizes in attaining higher performance. Large firms are more likely to exploit economies of scale and enjoy higher negotiation power over their clients and suppliers (Serrasqueiro and Macas Nunes 2008). In addition, they face less difficulty in getting access to credit for investment, have broader pools of qualified human capital, and may achieve greater
strategic diversification (Yang and Chen 2009). On the other hand, small firms exhibit certain characteristics which can counterbalance the handicaps attributed to their smallness. They suffer less from the agency problem and are characterised by more flexible non-hierarchical structures, which may be the appropriate organisational forms in changing business environments (Yang and Chen 2009).

Existing empirical evidence has not been unambiguous, lending support to both a positive and a negative impact of firm size on performance. Yang and Chen (2009) compared the technical efficiency of SMEs with that of large firms and were inconclusive about the relationship when choosing different estimation methods. In a study on Portuguese companies Serrasqueiro and Nunes (2008) found that size is related positively to performance but only for the sample of SMEs and not for large firms. A similar finding by Diaz and Sanchez (2008) in the Spanish context suggested that SMEs were more efficient than large firms lending support to earlier studies that identified an inverse relationship between size and performance (Hart and Oulton 1996). These studies imply a relationship between firm size and performance that might not necessarily be linear, as illustrated in Barrett et al. (2010), Yoon (2004), and Risseeuw (1997), which conclude that company growth beyond optimal level can deteriorate performance.

Jointly, existing studies suggest that small firms may face an incentive to grow with the prospect of exploiting various benefits attributed to larger size. A successful growth strategy would require a firm’s growth to not be seriously restricted by factorsexogenous to the firm. Namely, when forces outside managerial control confine the firm’s growth potential, increasing firm size might not be a realistic strategy to increasing performance. Firms operating in small economies can be highly exposed to such forces. Small economy size may limit the capacity of managers to implement a growth strategy and to some extremes challenge the long-term viability of the firm (Armstrong et al. 1998). Small economies are characterised by small local market sizes and their lack of economies of scale affects firms particularly in sectors where substantial fixed and sunk costs are prerequisites for operation. Moreover, their limited scope for skilled labour substantially reduces firms’ procurement options (Castello and Ozawa 1999). Small economies may sustain only a very small number of large firms, relative to the overall market size. Hence, they exhibit a predisposition towards monopolistic markets particularly in markets where the minimum efficient scale of operation (MES) of the firm is very close or larger than the total
market size. Notwithstanding a firm’s incentive to grow to improve its performance, economy size will restrain that potential, raising additional managerial challenges.

2.3.5 Firm Leverage

Though the Modigliani and Miller (1958) theorem suggested that the financial structure has no influence on firm value, a number of theoretical works have provided arguments in favor of the non-neutrality of financial structure in economic terms. Among the works contesting the relevance of Modigliani-Miller theorem, a major strand suggests a relation between leverage and corporate performance. The studies on the link between leverage and corporate performance can in fact be classified in two categories. The first one includes the works based on information asymmetries and signalling. Firm insiders (managers or shareholders) possess some private information about the characteristics of the firm. It has then been demonstrated that these information asymmetries between borrowers and lenders induce some adverse selection problems: the impossibility of lenders to price a loan according to the borrower’s quality results in an imperfect pricing, leading to credit rationing (Stiglitz and Weiss 1981).

Therefore, “high-quality” borrowers have incentives to show their quality. However, they need to provide this private information by using a credible signal, meaning a signal that cannot be provided by “low-quality” borrowers. Debt can then be adopted as this signal as the choice of financing by debt rather than by equity conveys valuable information to the lenders (Leland and Pyle 1977). In particular, Ross (1977) advanced that a “good-quality” company can issue more debt than a “low-quality” one, because the issue of debt leads to a higher probability of default due to the debt servicing costs which represent a costly outcome for firm insiders. As a result, debt is a credible signal of the quality of firms and “good-quality” firms are more inclined to issue debt. Thus, this theory suggests that the most performing firms, those having the more profitable investments, ask for more debt: there should then exist a positive relation between corporate performance and leverage.

Empirical evidence on the relation between leverage and performance is mixed; that is, the effect of leverage on performance has been found to be positive, negative, or insignificant. On the one hand, Margaritis and Psillaki (2010) find that leverage has a positive effect on firm performance. Cai and Zhang (2011) show that changes in financial leverage negatively affect stock returns. Similarly, Giroud et al. (2012) show that reducing leverage ratios result in better performance.
On the other hand, several scholars, such as Antoniou et al. (2008), provide evidence to support the notion that the relation between financial leverage and performance is negative. Furthermore, Connelly et al. (2012) find that the variation in leverage is not associated with firm performance, measured as Tobin’s q. Some studies show that the relation between financial leverage and firm performance is non-monotonic. For instance, Coricelli et al. (2012) find that the positive relation between leverage and total productivity growth exists to a certain point and beyond such a critical threshold, the negative relation between leverage and total productivity growth exists. In addition, financial leverage is associated with growth. For instance, Lang et al. (1996) find that leverage is negatively related with future growth. In other words, firms with higher leverage ratios appear to exhibit lower future growth rates.

2.4 Empirical Review
Within literature in different terms or in different sectors, there is a great number of studies carried out about ownership structure and business performance. In their study including the manufacturing firms operating in Tokyo stock exchange between the years of 1980 and 2005, Hu and Izumida (2008) have reached the conclusion that ownership concentration has a statistically meaningful effect on institutional performance in the current period and following period.

Clay (2001), who examined the relationship between institutional investor ownership and firm performance via 8951 businesses’ data between the years 1988 and 1999, identified that institutional investor ownership has a positive and significant effect on business performance. On the other hand, Charfeddine and Elmarzougui (2010) who made a similar research aimed at 35 businesses operand in France financial market between the years 2002 and 2005, identified that institutional investor ownership has a negative and significant effect on business performance. Along with this, Farooque, et al. (2007), defend the opinion that institutional investor ownership doesn’t have a significant effect on business performance.

Cornett et al (2007) in a research titled “the impact of institutional ownership on corporate operating performance” analyzed the relationship between institutional shareholders as one of the mechanisms of corporate governance and operational yield of large companies. They found a significant and positive relationship between the ratio of operating cash flow to sales as a measure of performance and the number and percentage of institutional shareholders as corporate governance mechanism.
Examining the effects of health institutions’ ownership structure over their financial performances, Alam et al (2008) designated five dimensions including nonfinancial performance, stabilization, capital structure, fixed asset efficiency and liquidity as an indication of performance. It is identified that there is a statistically meaningful difference between the performances of public hospitals and, profit oriented and non-profit hospitals in the analysis of data, which belong to the period covering the years 1980-2003.

Ezazi, et al. (2011) in a research titled “The effect of ownership structure on share price volatility of listed firm in Tehran Stock Exchange” examine the relation between them. The results of this research indicate that the price of shares of the companies whose more percentage of shares are held by their greatest shareholders may have more volatility and the share price volatility of the companies that the more percentage of their shares is held by individual shareholders is lower. It should be noted that the measure of ownership of five greater shareholders and institutional shareholders and members of the board of directors might not show any solution for investors interested in share price volatility.

Mang’unyi (2011) has examined the effects of ownership structure over institution management and performance in the sample of some selected banks operating in Kenya and revealed that there is a significant relationship between ownership structure and financial performance. The writer defends that banks that have foreign investor, in comparison with banks that have domestic investor, display a better performance. In the study (Uddin and Suzuki, 2011) aimed at the banks operating in Bangladesh between the years 2001 and 2008, similar results are obtained. Alimehmeti and Paletta (2012) on the other hand, examined the relationship between shareholder concentration and firm value in their study covering the years of 2006-2009. The writers have reached the conclusion that there is a positive sided statistical relationship between ownership concentration and firm value except for the crisis period (the period of 2008).

Warrad, et al (2013) examined the relationship between ownership concentration and business performance via the data of nonfinancial businesses that are listed on the stock exchange of Jordan between the years 1994 and 2005. In the study, two different group assessment criteria are determined as for accounting and market. According to accounting criterions it is concluded that ownership structure doesn’t have a significant effect on business performance, however
according to market criterions it is determined that ownership structure effects business performance significantly.

2.5 Summary of Literature Review
Many researchers have examined the relationship between ownership structure and firm performance. However, the results are mixed. Some examine only the impact of one aspect of ownership on performance, while others investigate the influence of several mechanisms together on performance. A yawning gap that exists since none of them covers effects of ownership structure on financial performance of firms in the stock market, specifically in the Kenyan Nairobi Securities Exchange. The studies done on the topic are highly conflicting and there is no clear direction of the effects. The accessible studies done on the topic is by Mang’unyi (2011) who focussed on governance practices related to ownership structure in the commercial banking sector in Kenya, and Ongore (2011), whom according to him, the concept of ownership can be defined along two lines of thought: ownership concentration and ownership mix. The concentration refers to proportion of shares held (largest shareholding) in the firm by few shareholders and the later defines the identity of the shareholders. It is against this background that the researcher found it necessary to carry out a study on ownership structure and its effects on financial performance of the firms operating in the Nairobi Securities Exchange to bridge the gap that exist.
CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction
This chapter presents the research design, target population, sampling design, data collection procedure, and procedures for data analysis.

3.2 Research Design
This study used descriptive survey design. A descriptive study attempts to describe or define a subject, often by creating profile of a group of problems, people, or events, through the collection of data and tabulation of the frequencies on research variables or their interaction, (Cooper and Schindler, 2006). The survey sought to obtain information that describes existing phenomena. It enabled the study to access comprehensive information to facilitate an establishment of the link between the ownership structures of all companies listed in the NSE and their financial performance.

3.3 Population
The sample population comprised all the sixty two (62) companies listed in the NSE as at August 2014. The study will conducted a census survey owing to the number of the companies listed on NSE (as provided in appendix i), being manageable. Therefore, the study targeted the whole population of the study.

3.4 Data Collection
The study required secondary data in meeting its obligation. Therefore, secondary data collection techniques was be employed. The study collected financial performance and shareholding information data as presented in their annual reports from the targeted institutions and data on financial performance was collected from the NSE within the study period 2009-2013. This data was analysed to facilitate meeting the study objective.

3.5 Data Analysis
The collected data was be examined for completeness and comprehensibility. The data was then coded and analysed using the Statistical Package for Social Sciences (SPSS Version 19) software. The study also employed inferential statistics such as regression and correlation to test
the relationship between ownership structure and firm performance in NSE firms. Data presentation was done by the use of frequency tables.

3.5.1 Analytical Model

The study will use the following regression model.

\[ FP_t = \alpha + \beta_1 OC_t + \beta_2 FO_t + \beta_3 IO_t + \beta_4 GO_t + \beta_5 DO_t + \beta_6 SZ_t + \beta_7 FL_t + \varepsilon_t \]

Where \( FP_t \) = Firm Performance as measured by ROE of company \( t \)

\( \alpha \) = Constant term

\( \beta_n \) = coefficients of \( i \)

\( OC \) = Ownership concentration as measured by shareholding above 30%

\( FO \) = Foreign ownership of company \( t \) as measured by shareholding percentage

\( IO \) = Institutional Ownership of company \( t \) as measured by shareholding percentage

\( GO \) = Government Ownership of company \( t \) as measured by shareholding percentage

\( DO \) = Diverse Ownership of company \( t \) as measured by shareholding percentage

\( SZ \) = Firm Size of company \( t \) as measured by market share

\( FL \) = Financial Leverage of company \( t \) as measured by gearing

\( \varepsilon_t \) = Error term

The relationship between ownership structure and firm performance is conceptualized based on pertinent literature on corporate governance. Ownership Structure will be conceptualized as comprising ownership concentration and ownership identity. Ownership concentration (shareholding above 30%) will be determined using Herfindahl Index, or the equity stake of several largest investors, typically the top five shareholders (Demsetz & Lehn, 1985). Four ownership categories identified as: foreign; institutional; government; and diverse will be considered. Each of these ownership identities has different risk-taking orientations, which in
effect affect investment decisions and firm performance differently. The data in this study will be analyzed using Pearson’s Product-Moment Correlation and Logistic Regression.

3.5.2 Test of Significance
Correlation will be used to test the relationship of the variables in the study. The study will also use ANOVA (model goodness of fit) to test the statistical significance of the variables in satisfying the set objectives, which will be calculated using SPSS software.
CHAPTER FOUR

DATA ANALYSIS, RESULTS AND DISCUSSION

4.1 Introduction
This chapter presents the data analysis, results, interpretation, and discussion of the research findings. To achieve the objective of the study, SPSS Version 17 statistical software was used to analyse the data. Linear regression was used to analyse the effect of ownership structures on financial performance of companies listed in the NSE County.

4.2 Response Rate
The sample population comprised all the sixty two (62) companies listed in the NSE as at August 2014. The study conducted a census survey owing to the number of the companies listed on NSE being manageable. Therefore, the study targeted the whole population of the study and collected audited financial statements and reports from the targeted companies within the study period 2009-2013. This data was analysed to facilitate meeting the study objective.

4.2 Descriptive Statistics
The study sought to determine the effect of ownership structures on financial performance of companies listed in the NSE. The references included audited financial statements and reports from the targeted companies within the study period 2009-2013.
Table 4.1: Descriptive Statistics

<table>
<thead>
<tr>
<th></th>
<th>FP (ROE)</th>
<th>OC</th>
<th>FO</th>
<th>IO</th>
<th>GO</th>
<th>DO</th>
<th>SZ</th>
<th>FL</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mean</td>
<td>0.205559</td>
<td>0.256445</td>
<td>0.277835</td>
<td>0.346969</td>
<td>0.024868</td>
<td>0.365458</td>
<td>0.287581</td>
<td>0.326561</td>
</tr>
<tr>
<td>SD</td>
<td>0.017303</td>
<td>0.016638</td>
<td>0.041616</td>
<td>0.034363</td>
<td>0.009056</td>
<td>0.030565</td>
<td>0.031683</td>
<td>0.02915</td>
</tr>
<tr>
<td>Median</td>
<td>0.218881</td>
<td>0.272</td>
<td>0.1035</td>
<td>0.31115</td>
<td>0</td>
<td>0.2937</td>
<td>0.18</td>
<td>0.2158</td>
</tr>
<tr>
<td>Mode</td>
<td>0.237</td>
<td>0.178</td>
<td>0</td>
<td>0.0502</td>
<td>0</td>
<td>0.2648</td>
<td>0.26</td>
<td>0.1382</td>
</tr>
<tr>
<td>SD</td>
<td>0.136247</td>
<td>0.131005</td>
<td>0.327688</td>
<td>0.261697</td>
<td>0.071305</td>
<td>0.240669</td>
<td>0.249476</td>
<td>0.22953</td>
</tr>
<tr>
<td>Min</td>
<td>0.106</td>
<td>0.106</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0.2623</td>
</tr>
<tr>
<td>Max</td>
<td>0.56</td>
<td>0.76</td>
<td>0.8848</td>
<td>0.7987</td>
<td>0.2623</td>
<td>0.9218</td>
<td>0.71</td>
<td>0.855</td>
</tr>
<tr>
<td>Kurtosis</td>
<td>3.712107</td>
<td>4.176136</td>
<td>-1.25753</td>
<td>-1.30595</td>
<td>7.976815</td>
<td>-0.29234</td>
<td>0.303241</td>
<td>-0.61668</td>
</tr>
<tr>
<td>Skewness</td>
<td>-1.02091</td>
<td>1.757209</td>
<td>0.718922</td>
<td>0.239397</td>
<td>3.095081</td>
<td>0.824006</td>
<td>1.426523</td>
<td>0.742201</td>
</tr>
<tr>
<td>Range</td>
<td>-0.306</td>
<td>0.106</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0.0332</td>
<td>0.09</td>
</tr>
<tr>
<td>Sum</td>
<td>12.74465</td>
<td>15.8996</td>
<td>17.2258</td>
<td>20.12418</td>
<td>1.5418</td>
<td>22.65842</td>
<td>17.83</td>
<td>20.24676</td>
</tr>
<tr>
<td>Count</td>
<td>62</td>
<td>62</td>
<td>62</td>
<td>58</td>
<td>62</td>
<td>62</td>
<td>62</td>
<td>62</td>
</tr>
</tbody>
</table>

Source: Research Findings

Table 4.1 above displays the descriptive statistics of the variables of interest across all the companies sampled. Eight variables namely financial performance, Ownership Concentration, Foreign Ownership, Institutional Ownership, Government Ownership, Diverse ownership, Size of the Company and Financial Leverage of the company with 5 observations each were used in the analysis. Financial performance had a mean of 0.205559 and a standard deviation of 0.017303. Its minimum value was -0.306 and maximum value was 0.56. This implies that on average, companies listed at the NSE enjoy a return on equity of about 20.56 percent.

Ownership concentration had a mean of 0.256445 and a standard deviation of 0.016638. Its minimum and maximum values are 0.106 and 0.76 respectively. Foreign Ownership had a mean of 0.277835 and a standard deviation of 0.041616. Its minimum and maximum values are 0 and 0.8848 respectively, implying that companies listed in the NSE have ownership of about 27.78 percent that is internationally owned. Institutional ownership had a mean of 0.346969 and a standard deviation of 0.034363. Its minimum and maximum values are 0.0173 and 0.7987 respectively. Government ownership had a mean of 0.024868 and a standard deviation of 0.009056. Its minimum and maximum values are 0 and 0.2623 respectively, implying that the government rarely participates. Diverse ownership had a mean of 0.365458 and a standard deviation of 0.030565. Its minimum and maximum values are 0.0332 and 0.955 respectively.
Financial leverage had a mean of 0.326561 and a standard deviation of 0.02915. Its minimum and maximum values are 0.025 and 0.88 respectively.

4.3 Correlation Matrix

Table 4.2: Correlation Matrix

<table>
<thead>
<tr>
<th></th>
<th>FP (ROE)</th>
<th>OC</th>
<th>FO</th>
<th>IO</th>
<th>GO</th>
<th>DO</th>
<th>SZ</th>
<th>FL</th>
</tr>
</thead>
<tbody>
<tr>
<td>FP (ROE)</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>OC</td>
<td>0.309001</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>FO</td>
<td>0.083395</td>
<td>0.422206</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>IO</td>
<td>-0.34742</td>
<td>-0.40342</td>
<td>0.63072</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>GO</td>
<td>0.130911</td>
<td>-0.22609</td>
<td>-0.04132</td>
<td>-0.16647</td>
<td>1</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>DO</td>
<td>0.117823</td>
<td>-0.03764</td>
<td>-0.57746</td>
<td>-0.28814</td>
<td>-0.06634</td>
<td>1</td>
<td></td>
<td></td>
</tr>
<tr>
<td>SZ</td>
<td>0.255374</td>
<td>0.332839</td>
<td>-0.11176</td>
<td>-0.22704</td>
<td>-0.14586</td>
<td>0.368291</td>
<td>1</td>
<td></td>
</tr>
<tr>
<td>FL</td>
<td>-0.12413</td>
<td>-0.21483</td>
<td>-0.3759</td>
<td>0.502195</td>
<td>-0.12085</td>
<td>-0.07713</td>
<td>0.026698</td>
<td>1</td>
</tr>
</tbody>
</table>

Source: Research Findings

An assessment of the extent of correlation among the variables used in the study has been done using a correlation matrix as shown in Table 4.2. Each variable is perfectly correlated with itself as indicated by the coefficient of 1. This matrix attempts to provide insights on the hypothesis tests that the study intended to test. The correlation between firm leverage and financial performance is negative suggesting that profitable firms in the NSE tend to borrow less. It can be observed that we cannot reject the null hypothesis that there is no significant effect of ownership structures on financial performance of companies listed in the NSE.

4.4 Pooled OLS Regression Model

The empirical analysis was conducted on the whole population of the companies listed in the Nairobi Securities Exchange using the linear regression analysis method.

4.4.1 ANOVA table

The study used ANOVA statistics to establish the significance of the relationship between financial performance and the independent variables. The regression model is not significant given the level of significance $F(7,50) = 1.9$, $p = 0.082$ which is above 0.05, therefore there is no statistical significant difference between the means of the dependent and independent variables.
Table 4.3. Analysis of Variance (ANOVA)

<table>
<thead>
<tr>
<th>Model</th>
<th>Sum of Squares</th>
<th>df</th>
<th>Mean Square</th>
<th>F</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Regression</td>
<td>.220</td>
<td>7</td>
<td>.031</td>
<td>1.941</td>
<td>.082</td>
</tr>
<tr>
<td>Residual</td>
<td>.811</td>
<td>50</td>
<td>.016</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>1.032</td>
<td>57</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

a. Predictors: (Constant), Financial Leverage, Size of Company, Government Ownership, Foreign Ownership, Ownership Concentration, Diverse Ownership, Institutional Ownership
b. Dependent Variable: Financial Performance

Source: Research Findings

4.4.2 Model Fit

Determination of coefficients (R^2) were also carried out to determine the strength of the relationship between independent and dependent variables. The study established an R square of 0.214. This implies that 21.4% of the financial performance of companies listed in the NSE is attributed to changes independent variables. The Durbin-Watson test statistic tests the null hypothesis that the residuals from an ordinary least-squares regression are not auto correlated. The Durbin-Watson statistic ranges in value from 0 to 4. A value near 2 indicates non-autocorrelation; a value toward 0 indicates positive autocorrelation; a value toward 4 indicates negative autocorrelation. Since the Durbin-Watson value of 1.816 was close to 2, then it can be concluded that there was no autocorrelation among the model residual.

Table 4.4 Goodness of fit statistic

<table>
<thead>
<tr>
<th>Model</th>
<th>R</th>
<th>R Square</th>
<th>Adjusted R Square</th>
<th>Std. Error of the Estimate</th>
<th>Durbin-Watson</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>.462a</td>
<td>.214</td>
<td>.104</td>
<td>.1273746</td>
<td>1.816</td>
</tr>
</tbody>
</table>

a. Predictors: (Constant), Financial Leverage, Size of Company, Government Ownership, Foreign Ownership, Ownership Concentration, Diverse Ownership, Institutional Ownership
b. Dependent Variable: Financial Performance

Source: Research Findings
4.4.3 Coefficients of the Model

Multiple regression analysis was used to determine the significance of the relationship between the dependent variable and all the independent variables pooled together. The results are given in the model summary in Table 4.5 below.

Table 4.5 Regression Result

<table>
<thead>
<tr>
<th>Model</th>
<th>Unstandardized Coefficients</th>
<th>Standardized Coefficients</th>
<th>t</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 (Constant)</td>
<td></td>
<td></td>
<td>-0.547</td>
<td>0.709</td>
</tr>
<tr>
<td>Ownership Concentration</td>
<td>0.191</td>
<td>0.164</td>
<td>0.192</td>
<td>1.164</td>
</tr>
<tr>
<td>Foreign Ownership</td>
<td>0.742</td>
<td>0.725</td>
<td>1.630</td>
<td>1.024</td>
</tr>
<tr>
<td>Institutional Ownership</td>
<td>0.624</td>
<td>0.714</td>
<td>1.213</td>
<td>0.874</td>
</tr>
<tr>
<td>Government Ownership</td>
<td>0.987</td>
<td>0.721</td>
<td>0.541</td>
<td>1.370</td>
</tr>
<tr>
<td>Diverse Ownership</td>
<td>0.708</td>
<td>0.719</td>
<td>1.253</td>
<td>0.985</td>
</tr>
<tr>
<td>Size of Company</td>
<td>0.057</td>
<td>0.077</td>
<td>0.108</td>
<td>0.742</td>
</tr>
<tr>
<td>Financial Leverage</td>
<td>0.024</td>
<td>0.091</td>
<td>0.042</td>
<td>0.264</td>
</tr>
</tbody>
</table>

a. Dependent Variable: Financial Performance

Source: Research Findings

From the regression result, the estimated model is given below:

\[ FP = -0.547 + 0.191OC + 0.742FO + 0.624IO + 0.987GO + 0.708DO + 0.057SZ + 0.024FL \]

At 5% level of significance all the variables are not statistically significant in explaining the variation in financial performance of the companies listed in the NSE.

4.5 Interpretation of the Findings

From the results, ownership concentration is positively related to the measures of performance in firms listed at the NSE. These results are consistent with the previous studies’ findings by Berle and Means (1932) who studied ownership structure and firm performance and found that company’s ownership concentration had a statistically positive relationship with firm performance at 5% significance level while controlling for the firm’s size, financial leverage, systematic risk and industry. The study found that there is an insignificant positive relationship
between manager-controlled firms (as opposed to owner-controlled) and a high variance in profit/equity. This positive effect means that higher ownership concentration has both the ability and the incentive to monitor and control agents, in order to operate the firm for the good of the shareholders.

A negative relationship between firm performance and financial leverage in listed Kenyan companies is a vindication of pecking order theory i.e. more profitable companies prefer to finance their investment activities using retained earnings as opposed to external financing. A company may opt for this policy in order to maintain its financial flexibility and to minimize the amount of information available to outsiders. According to Myers and Majluf (1984), firms follow a pecking order in their financing choice in order to minimise underinvestment problems and project mispricing.

The factors that significantly enhance firms’ return on equity include Company’s ownership concentration, foreign ownership and size of the company, and institutional ownership and financial leverage of the company significantly undermines the return on equity. This result are consistent with the previous studies’ findings by Antoniou et al. (2008) that show that changes in financial leverage negatively affect returns.

One of the assumptions of the classical regression is that the disturbances in the model are not auto correlated. Another way of stating this assumption is that the correlation between disturbances from different observation period is zero. To test for serial correlation, we used the Durbin-Watson test. The rule of thumb for this test is that if d is found to be 2 in an application, one may assume that there is no first-order autocorrelation, either positive or negative. This also implies that the closer the statistic is to 2, the better. Specifically, the Durbin-Watson statistic will fall below 2 if there is positive serial correlation (in the worst case, it will be near zero) and lie between 2 and 4 if there is negative correlation. All the three models seem to meet this threshold hence no autocorrelation.
CHAPTER FIVE

SUMMARY, CONCLUSION, AND RECOMMENDATIONS

5.1 Introduction
This chapter presents the summary of finds, conclusion, recommendations and suggestions for further research derived from the findings. The chapter also presents the limitations that were encountered with suggestions for further research.

5.1 Summary
The objective of the study was to determine the effect of ownership structures on financial performance of companies listed in the NSE. The study intended to enhance understanding on the issue by finding out how the financial performance is affected by the ownership structures.

To achieve this objective, all the sixty two (62) companies listed in the NSE as at August 2014 for the period 2008-2012 were sampled. The estimation results revealed that the financial performance of companies listed at the NSE during this period enjoyed a return on equity of about 20.56 percent. The estimation results further revealed that Ownership concentration had a significant effect on financial performance. Foreign ownership and size of the company also had a positive effect on a company’s financial performance.

The results further revealed that financial leverage had a negative effect on the financial performance of the companies listed in the NSE. These findings are consistent with findings in most of developed countries despite profound difference in institutions and macroeconomic environment.

5.2 Conclusion
The study findings lead us to make conclusions and draw important policy implications. First, the financial performance of a company cannot be directly attributed to the ownership structure. In theory, the ownership concentration of the companies listed in the NSE does positively affect the financial performance, but there are other factors that affect it that were not included in the model. The implication is that when more than 30 per cent or more of shares are concentrated on a few hands (i.e. five shareholders or less), there is a tendency for the shareholders to be overzealous in their monitoring, controlling and ratification roles over managers.
There is a positive relationship between diverse ownership and firm performance. Diverse ownership mainly consists of the public and the managers of the companies. It has been argued that when managers own shares in their company, they become more committed to the organization since they have a stake in the residual income of the firm, and are likely to bear the cost of mismanagement. This commitment translates to superior performance. This stifles managers’ creativity and innovation, and ultimately affects firm performance adversely.

Further, the firms in listed in the NSE seem to follow pecking order theory which is based on assumption of asymmetry of information. This being the case it then follows that the degree of asymmetry in Kenya may be quite high, the government should therefore make a deliberate effort to minimise asymmetry in the country as this could cause market failure. In this regard the government can use various signalling devices to bring confidence into the market.

The study also shows that the level of financial leverage and government ownership negatively affects the financial performance of a company. This is in line with several other studies carried out in the NSE.

5.3 Recommendations for Policy & Practice

The study findings lead us to make important policy implications. First, the financial performance of a company cannot be directly attributed to the ownership structure. In theory, the ownership concentration of the companies listed in the NSE does positively affect the financial performance, but there are other factors that affect it that were not included in the model. The implication is that when more than 30 per cent or more of shares are concentrated on a few hands (i.e. five shareholders or less), there is a tendency for the shareholders to be overzealous in their monitoring, controlling and ratification roles over managers. The results of the current study have therefore, shown there is dire need to reasonably diversify shareholding as a way of attracting more skills and competencies among the shareholders that can be tapped to improve firm performance. At the same time, the managers should be protected from unnecessary direct interference by the shareholders.

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5.4 Limitations of the study

In carrying out this study, a limitation relating to the measurement of financial leverage was noted. In this regard, Gearing was used to measure the financial leverage of the firms listed in the NSE. However, financial leverage could be measured using other financial ratios such as debt ratio, working capital ratio, current ratio, among many others.

Also, another limitation relating to the measurement of financial performance was noted. In this regard, ROE was used to measure the financial performance of the companies in the study. However, financial performance could be measured using market ratios such as price earnings ratio, market yield ratio among others.

A limitation also arose with the measurement of the size of the company. The measure used for this was percentage of market share. Other measures that could be used include annual turnover.

Lastly, getting recent financial records for some companies was impossible as they had not posted them on their websites nor had they made them available to the Capital Markets Authority. It is possible that if any of those ratios were included in the study, the results would have been different.
5.5 Suggestions for Further Research

Future studies should be conducted to establish the critical level of shareholding, beyond which there would be accelerated firm performance arising from commitment of managers.

Also, based on the limitations explained, we recommend that future studies be carried out with the size of the company measured by the annual turnover.

Further studies should also be conducted to establish the effects of ownership identity on financial performance of a company listed in the NSE, i.e. separate from ownership concentration.
REFERENCES


Adrian Vinuales, (2014). Market returns in Kenya,


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APPENDICES

Appendix 1: Quoted Firms in Nairobi Securities Exchange

AGRICULTURAL

1. Eaagads Ltd
2. Kapchorua Tea Co. Ltd
3. Kakuzi
4. Limuru Tea Co. Ltd
5. Rea Vipingo Plantations Ltd
6. Sasini Ltd
7. Williamson Tea Kenya Ltd

COMMERCIAL AND SERVICES

8. Express Ltd
9. Kenya Airways Ltd
10. Nation Media Group
11. Standard Group Ltd
12. TPS Eastern Africa (Serena) Ltd
13. Scangroup Ltd
14. Uchumi Supermarket LTD
15. Hutchings Biemer Ltd
16. Longhorn Kenya Ltd

TELECOMMUNICATION AND TECHNOLOGY

17. Access Kenya Group Ltd
18. Safaricom Ltd

AUTOMOBILES AND ACCESSORIES

19. Car and General (K) Ltd
20. CMC Holdings Ltd
21. Sameer Africa Ltd
22. Marshalls (E.A.) Ltd
BANKING

23. Barclays Bank Ltd
24. CFC Stanbic Holdings Ltd
25. I&M Holdings Ltd
26. Diamond Trust Bank Kenya Ltd
27. Housing Finance Co Ltd
28. Kenya Commercial Bank Ltd
29. National Bank of Kenya Ltd
30. NIC Bank Ltd
31. Standard Chartered Bank Ltd
32. Equity Bank Ltd
33. The Co-operative Bank of Kenya Ltd

INSURANCE

34. Jubilee Holdings Ltd
35. Pan Africa Insurance Holdings Ltd
36. Kenya Re-Insurance Corporation Ltd
37. CFC Insurance Holdings
38. British-American Investments Company (Kenya) Ltd
39. CIC Insurance Group Ltd

INVESTMENT

40. Olympia Capital Holdings Ltd
41. Centum Investment Co Ltd
42. Trans-Century Ltd

MANUFACTURING AND ALLIED

43. B.O.C Kenya Ltd
44. British American Tobacco Kenya Ltd
45. Carbacid Investments Ltd
46. East African Breweries Ltd
47. Mumias Sugar Co. Ltd
48. Unga Group Ltd  
49. Eveready East Africa Ltd  
50. Kenya Orchards Ltd  
51. A.Baumann CO Ltd  

CONSTRUCTION AND ALLIED  
52. Athi River Mining  
53. Bamburi Cement Ltd  
54. Crown Berger Ltd  
55. E.A.Cables Ltd  
56. E.A.Portland Cement Ltd  

ENERGY AND PETROLEUM  
57. KenolKobil Ltd  
58. Total Kenya Ltd  
59. KenGen Ltd  
60. Kenya Power & Lighting Co Ltd  
61. Umeme ltd  

GROWTH ENTERPRISE MARKET SEGMENT  
62. Home Africa ltd  

Source: NSE website (https://www.nse.co.ke/) accessed on 4th September 2014