EFFECTS OF BOARD DIVERSITY ON FINANCIAL PERFORMANCE OF COMMERCIAL BANKS IN KENYA

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DECLARATION

This research project is my original work and has not been submitted for an award of degree, diploma or certificate at any university or college.

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DEDICATION

To my family whose support and most of all love they have given me to endure through my study.

TABLE OF CONTENTS

DECLARATION ..... **ii**

ACKNOWLEDGEMENT ..... **iii**

DEDICATION ..... **iv**

LIST OF TABLES ..... **vii**

ABBREVIATIONS ..... **viii**

ABSTRACT ..... **ix**

CHAPTER ONE: INTRODUCTION **1**

1.1 Background of the Study 1

1.1.1 Board Diversity 2

1.1.2 Financial Performance 3

1.1.3 Board Diversity and Financial Performance 4

1.1.4 Commercial Banks in Kenya 5

1.2 Research Problem 6

1.3 Research Objective 8

1.4 Value of the Study 8

CHAPTER TWO: LITERATURE REVIEW **9**

2.1. Introduction 9

2.2. Theoretical Review 9

2.3 Determinants of Financial Performance of Commercial Banks 12

2.4 Empirical Literature 16

2.5 Conceptual Framework 21

2.6 Summary of Literature Review 22

CHAPTER THREE: RESEARCH METHODOLOGY 23
3.1 Introduction 23
3.2 Research Design 23
3.3 Population 23
3.4 Data Collection and Description 24
3.5 Data Analysis 24
3.6. Test of Significance 26
CHAPTER FOUR: DATA ANALYSIS, INTERPRETATIONS AND PRESENTATION 27
4.1. Introduction 27
4.2 Descriptive Statistics 27
4.3 Correlation Analysis 28
4.4 Regression Analysis 29
4.5 Discussion of the Findings 31
CHAPTER FIVE: SUMMARY, CONCLUSION AND RECOMMENDATIONS 33
5.1 Introduction 33
5.2 Summary 33
5.3 Conclusions 34
5.4 Recommendations 35
5.5 Limitations 36
5.6 Suggestions for Further Research 36
REFERENCES 37
APPENDICES 45
Appendix I: List of Banks 45
Appendix II: Education Levels 47
Appendix III: Commercial Banks Data 48

LIST OF TABLES

Table 4.1:Correlation Table 28

Table 4.2: Model Summary 29

Table 4.3: ANOVA 30

Table 4.4: Coefficients Table 30

ABBREVIATIONS

CBK…… Central Bank of Kenya

EBIT……Earnings before interest and tax

EU………European Union

NSE……..Nairobi Securities Exchange

OECD…...Organization for Economic Cooperation and Development

OLS……..Ordinary Least Square

ROA…… Return on Assets

ROE……. Return on Equity

SME……..Small and Medium-Sized Enterprise

USA……..United States of America

USD……..United States Dollar

ABSTRACT

Composition of any firms' board plays a key role in determining the firm financial performance. Findings suggest that there is a substantial influence of different boards' qualities on firm financial performance. No sufficient exploitation study has been carried out on the impact of board diversity on the financial performance of commercial banks in Kenya. This study thus looked to close the gap by determining the effect of board diversity on the financial performance of commercial banks in Kenya. This study considered causal research design. The objective populace for this study was all the 42 commercial banks in Kenya for 5 years. The data pertaining to age, gender and education levels of the board members was collected from audited annual reports of the listed commercial banks. Information on financial performance was promptly accessible in secondary sources that incorporated financial information from financial statements of the commercial banks. These included the Nairobi Securities Exchange (NSE) annual publications, the NSE Handbook (2009), the banks' annual reports, and the Central Bank of Kenya website. Regression analysis was applied to evaluate the link between the top managements' diversity and banks financial performance. This study clearly proved to be that directors' age, average period of experience, gender and education level has a positive relationship with the banks financial performance. The study conclusions brought it out plainly that diversity could be a vital corporate governance element in other business sides rather than to boardrooms. Whatever measure could be put to use to enhance individuals selected as directors in terms of their age, average period of experience, gender and education level may positively influence the performance of commercial banks. The study also concluded that there is a gender issue in the board composition in many banks. These findings could resemble as the greater part of the boards are male lead and the couple of women existing on the board might not have any effect on the bank strategies. Commercial Banks should therefore have a satisfactory and diverse board size designed so as to ensure diversity of experience without yielding freedom, similarity, honesty and availability of individuals to go to meetings. The board size ought not to be excessively vast and ought to be comprised of qualified experts who are familiar with the oversight function. The number of non-executive and independent directors needs to be selected with a lot care since they affect financial performance commercial banks. The board needs to consist of well-educated and experienced professionals since they are actively involved in modeling the decisions of financial institutions. Last but not least, commercial banks who value return on assets should have their board members serving for a shorter term and have more board members experienced in banking. Banks focusing on improving return on assets should reduce the board size and increase the ratio of female members in the board.

CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

The board of directors is usually a form of control mechanism used by organizations internally to control the appointment, supervision and remuneration of top management in institutions besides strategy formulation (Minguez & Campbell, 2010). It is known fact that the board composition plays a key role in determining the firm financial performance (Ujunwa, 2012). Scholars, professionals and policy makers have throughout the previous two decades discussed on the role of boards as one of the key pillars of corporate governance (Tricker, 2009). For a long time, the role of the board as a pillar of corporate governance has elicited a debate between practitioners and policy makers. Some scholars argue that different board of directors attributes impact organizational performance owing to different orientations. The most common board of directors' attributes includes gender, age, education, and corporate experience (Letting, Aosa & Machuki, 2012). Boards constituted under subjective circumstances can serve or fail to be objective with the interests of the organization.

A majority of the boards constituted in organizations based in Kenya are usually male dominated as the appointments are done through closed networks whereby the male directors introduce their associates to boards before their term expires (Ekadah and Mboya, 2011). Such appointments prove detrimental to many women who seek opportunities with corporate boards hence depriving the organization of women (Ekadah and Mboya, 2011). A majority of studies conducted on the impact of board diversity on the financial performance of organizations have not focused on

Commercial Banks in Kenya. The study focuses on al Commercial Banks in Kenya owing to the limited research in this sector of the economy and the fact that secondary data of the banks is readily available in the NSE and Central Bank websites.

1.1.1 Board Diversity

Board diversity is the proportion of women, ethnic, racial minorities (people who are not Anglo- Australians) on the board (Wang and Cliff, 2009). Board diversity in age distribution, gender, physically impaired, type of educational qualification and other forms of diversity on corporate boards world-wide has been a subject of debate and study for some time now. Numerous organizations have undertaken campaigns to increase the number of women, people of different ethnic, social or racial orientations and the younger age groups through a focus on corporate governance, diversity standards and metrics and networking for progress. There has been a steady, albeit incremental increase in the presence of women on corporate boards since 2008 (Chanavat & Ramsden, 2013).

Freeman (1984) analyzed board assorted qualities from a gender, minor and ethnic point of view whereby he incorporates assortments of board aptitudes while Marimuthu (2008) clarified that a diverse group is characterized as being female, African American, Asian, and Hispanic which concurred with Freeman (1984). Corporate boards are a product of director attributes, diverse perspectives, business experiences, and skill sets that are deemed suitable for the relevant organization. Core attributes of board directors should address management experience, accounting or finance, industry knowledge, customer-care experience, disaster response, leadership as well as strategic planning. Freeman (1984) is of the view that diversified boards are more beneficial compared to the non-diversified ones.

1.1.2 Financial Performance

Financial performance is simply outlined in output terms as the accomplishment of quantified objectives (2006). Firm performance is a multidimensional hypothesis that consists of four components (Alamet, 2011): Human resource execution, containing employee fulfillment; firm profitability, for example, time to market, level of innovation, and supply chain adaptability; client based performance, such as consumer loyalty, and product or service execution ;financial and economic performance, including returns, market position, revenue, earning per share and cash-to-cash cycle time.

Market based measures of company's execution were completed by Shah et al. (2011) such that monetary reporting was measured by ROE and Return on investment (net return + premium)/ (value +total debt). Bhagat and Black (1999) measured dependent variable firm execution by return on assets (Operating income/assets), Turnover ratio (Sales/Assets), Operating margin (Operating income/Sales), Sales per worker, Growth of Assets, Sales, Operating income, Employees and Cash flows.

This research will focus on those measures that are crucial for the accomplishment of the commercial banks objectives. Therefore, this study would compute the financial performance of the banks by focusing on output (Return on Assets, Return on Equity and Dividend Yield). Return on Assets (ROA) indicates to the measure of net profit returned as a rate of total assets. It can be divided into: Return on Assets= EBIT/Average total assets in book value while Return on Equity (ROE) alludes to the measure of net pay returned as a rate of stockholder's equity. Return on equity measures an organization's profitability by determining the amount of profit a bank produces with the funds contributed by shareholders.

1.1.3 Board Diversity and Financial Performance

Allen, Gail and Wheatley (2008) and Marimuthu (2008) are of the view that diversity provides positive performance benefits to organizations. Fan (2012) concur with the finding that there is a positive correlation between gender of board members and Tobin's Q as a ratio of financial execution. Allen (2008) established that organizational performance is linked critically to the diversity within the senior management and non- managerial levels of an organization. Prihatiningtias (2012) used Return on Assets (ROA) and Tobin's Q to measure financial performance and noted that gender diversity had both adverse and affirmative effects on the financial execution of the firm.

This is contrary to Schwizer et, al. (2012) who studied the boards in Italy between the years 2006 to 2008 and found no statistical relationship between the presence of female directors on the boards of firms listed in the Italian Stock Exchange and firm financial performance. Mwatsuma, Muchiri and Mrope (2012) noted an adverse relationship between the number of board members and the performance of Agricultural organizations in Kenya. It is concluded that despite the general perception of the affirmative association between several forms of board diversity and firms' financial execution, studies conducted worldwide have shown mixed findings. This calls for further research in this area especially in the African and particularly the Kenyan context where fewer research efforts have been directed to determine the relationship.

1.1.4 Commercial Banks in Kenya

Commercial banks in Kenya play a major role in Kenya. They add to the financial development of the nation by availing resources for investments in addition to financial deepening in the nation. Commercial banks thus play a vital role in the state's economy. In this study, all commercial banks are used because of the availability of information on their performance through their annual reports which are available freely to the public. Bank financial performance in the past has significantly improved since 2000. Data retrieved from the CBK database shows an improvement of growth and financial performance of all industries. While this is the case, some banks, especially the foreign banks, have been performing better than others.

Diversity enhances the effectiveness of a board, particularly its capability to participate in problem-solving and strategic execution .Accordingly, boards in corporate banks are viewed as learning-based resource which adds significance for stockholders by connecting an organization to its external environment .Owing to their unconventional skills and values, different board members deliver constrained economic resources to organizations which assist in the understanding of the bank's dynamic industry. To further an organization's understanding of its industry and improve corporate performance, the presence of skills and knowledge is required to cater to boards' expert needs especially when boards match their diversity to that of customers and suppliers. The diversity found in boards may also provide improved access to capital more so for companies that operate in a regulated industry such as banking and capital markets. Therefore, board diversity creates shareholder value in corporate governance in the market.

1.2 Research Problem

It is a well-known fact that the composition of any firms' board plays a key role in determining the firm financial performance (Ujunwa, 2012). Scholars as well as policy makers have for a long time argued on the importance of boards as one of the vital pillars of corporate governance (Tricker, 2009). Some scholars argue that different board of director's traits impact the financial performance owing to different orientations. The most common board of directors' attributes includes gender, age, education, and corporate experience (Letting, Aosa & Machuki, 2012).

Despite proper regulatory framework, effective board administration remains weak in Kenya (Mangunyi, 2011). As per Mureithi, (2009), numerous organizations have been hit by scandals since board individuals have acted unlawfully or in lacking honesty towards their stockholders. The lack of professional management and governance malpractices has seen some banks experience significant financial difficulties forcing Central Bank to place them under statutory management. For example, the recent collapse of commercial banks in Kenya such as Chase Bank, Imperial Bank, Euro Bank, Dubai Bank, Kenya Finance Corporation, Trade Bank and Charter House bank among others. Chase Bank, which had established itself as the gem among small and medium-sized enterprise (SME) lenders in the market, and attracted funding from big international investors, collapsed in 2016. While Chase bank transferred the blame towards the accounting surrounding the bank's Islamic banking assets, more serious implications point towards governance problems. For instance, the bank made staggeringly large amount of loans to its directors, an average of KES 1.35 billion per director (USD 13.5 million).

In addition, the recent events in the global scene concerning high-profile corporate failures such as Enron in the US have intensified debate on the efficacy of board diversity as a means of increasing corporate financial performance. However, the available literature on the association between board diversity and firm financial execution reveals varied results. Studies have been conducted on the impact of board diversity on the performance of firms listed in the Nairobi Securities Exchange. For example, Letting, Aosa and Machuki (2012) looked at the impact of boards on the performance of the microfinance firms in Tanzania and Kenya while Neema and Olomi (2012) studied the impact of designated corporate governance aspects on firm's performance in Kenya. Aduda et, al. (2013) conducted an experiential test on opposing corporate governance theories on the performance of companies listed at the Nairobi Securities Exchange. Findings suggest that there is a substantial influence of different boards' qualities on firm financial performance. The finding is of great significance for stakeholders and policy makers that will act as reference for enhanced investment resolutions.

No sufficient exploitation study has been carried out on the impact of board diversity on the financial performance of commercial banks in Kenya. This study therefore sought to close the gap by determining the effect of board diversity on the financial performance of commercial banks in Kenya. The research on the executives' diversity and financial performance of banks would help various company shareholders, Government of Kenya, the Central Bank and foreign investors in the Kenyan capital market understand the relationship between diversity and organizational financial success.

1.3 Research Objective

The objective of this study was to determine the effects of board diversity on financial performance of commercial banks in Kenya.

1.4 Value of the Study

Prior studies carried out on the correlation between board diversity and financial execution has concentrated on mostly developed countries. For example, in Europe, Germany and lately Italy, Australia and the U.S.A have passed legislation concerning the number of female board members. The field of board diversity and its bearing on financial performance holds a lot of potential in further academic research. This study will assist future researchers in providing reference materials with regards to the banking sector in developing countries like Kenya.

The findings of this study will contribute pertinent information regarding board composition of firms in the economy and the impact of board diversity attributes in relation to stockholders' aim of maximizing their wealth as measured using the measurement variables discussed in the study. This material will accord financial establishments, advisers and businesspersons with the necessary gears to enhance the financial performances of their companies. In addition, these conclusions will provide data that will act as a guide to the Kenyan Government in relation to the possible need for legislation for the gender composition in the corporate boards. It will also provide a base for further investigation in corporate governance theories targeting emerging countries as most studies in this field have been concentrated in the developed countries.

CHAPTER TWO

LITERATURE REVIEW

2.1. Introduction

This chapter ponders on the literature related to the effect of board diversity on financial execution of commercial banks. Its presentation starts with the theoretical literature then empirical literature and the researcher's conclusion. According to Mugenda and Mugenda (2003), Literature analysis involves the systematic identification, position and examination of documents containing data linked to the study problem being examined.

The objective is to gain a deeper understanding of the past, development and direction which provides justification in revealing the knowledge gap necessitating this study.

2.2. Theoretical Review

This section assesses the various theories related to Board Diversity. This includes the Agency theory, Stewardship theory and Shareholders theory.

2.2.1. The Agency Theory

The agency relationship as depicted by Jensen and Meckling (1976) argues that in firms where equity is widely held, managerial actions tend to depart from the requirements of shareholders which are to maximize their wealth, this creates the agency problem. The theory holds the proposition that in the presence of information asymmetry, agent actions may end up hurting the owners. Eisenhardit (1989) states that the office agency problems emerge when the wishes or objectives of the principal and agents' strife and when it is hard or expensive for the principal to determine the agents' operations.

The concern is that the principal can't check that the agent is acting properly and to his greatest advantage. According to Shleifer and Vishny (1997), office issues can be sorted out with regards to a businessman or manager who raises monies for entrepreneurs to put them into favorable use. Nevertheless, by what means can the financiers make certain that once they sink their assets they will get everything again from the manager?

Jensen and Meckling (1976) explained how entrepreneurs in publicly listed companies bring about expenses in checking and holding managers to the best interest of shareholders. They characterized the organization costs just like the total of expenses of monitoring management (agent); bonding the agent to the principal (shareholder): and the owing losses. As indicated by Fama and Jensen (1983) the unmistakable ramifications of corporate governance from the agency hypothesis viewpoint is that monitoring and control mechanisms should be formed to shield stakeholders from management conflict of interest. As per the agency perspective, Boards of Directors are set up to screen management for the benefit of shareholders (Eisenhardt, 1989; Jensen and Meckling, 1976).

Agency issue may influence the estimation of an organization through two ways; the expected cash flows amassing to the organization and the cost of investment. Jensen (1986) proposes a theory that great administration lessens the assets under the control of managers and in an indirect way diminishes the chance of misappropriations by directors, likewise great administration diminishes the cost of capital either through the reduction of shareholders monitoring and appraisal costs. The share price that the shareholder (principal) pays reveals such agency costs. To magnify firm value one should balance the organization costs against the benefits anticipated that would accumulate to the firm by acquiring such expenses.

2.2.2. Stewardship Theory

Stewardship hypothesis states that executives are great stewards of enterprises and resolutely work to accomplish high measures of corporate returns and stockholders' earnings (Donaldson and Davis, 1994). One of the requisites of business law is that boards ought to demonstrate fiduciary duty to the stockholders of the firm. This depends on the supposition that directors having fiduciary duty can be trusted and will go about as stewards over the assets of the organization. Along these lines the obligations of a director are based on stewardship hypothesis which is a higher obligation than that of an agent as the individual must go about just as he were the director instead of a representative of the principal.

Donaldson and Davis (1994) further indicates that managers are basically driven by achievements and accountability need and along these lines, given the requirements of supervisors for capable, self-coordinated work; associations perhaps better served to free administrators of organizations from subservience to non-official executive controlled boards. Underlying this hypothesis is the evidence that since directors are normally dependable there will be no major agency costs (Donaldson, 1990; Danaldson & Preston, 1995). Stewardship scholars additionally contend that senior officials will not inconvenience shareholders for fear of jeopardizing their repute (Donaldson and Davis, 1994). Advocates of stewardship hypothesis contend that the board ought to have a noteworthy extent of inside executives to guarantee more successful and effective basic leadership.

2.2.3. Stakeholder Theory

According to Clarkson (1994), stakeholder theory states that the firm is network of stakeholders functioning within the larger circle. This theory states that administrators should choose choices that take into account the concerns of all the firm stockholders.

Supporters of such an outlook resist, to the point that the current firms' constraints on administrative conduct, for example, non-official executives, the review procedure, the threat of buyout, are lacking to avert managers mishandling corporate supremacy. Shareholders protected by liquid asset markets are apathetic to everything with the exception of the most substantial of exploitations. The objective of corporate governance is to magnify the wealth creation of the company altogether (Clarkson, 1994).

In particular, a stakeholder is characterized as "any gathering or person who can influence or is influenced by the accomplishment of the association's goals" (Freeman, 1984,), and this is "intended to sum up the idea of stockholders as the main group to whom management should be responsive" (Freeman, 1984). These classifications form the premise that the modern-day firm is predisposed to vested parties such as stockholders, consumers, bankers, staff, merchants and administration, who are commonly mentioned to as the essential stockholders, who are known to be crucial to the existence and success of the organization. To these the establishment includes secondary stockholders, for instance, the media, the government, the courts, specific vested parties and the general public, that is whole society in general. From this point of view, corporate governance talks about frequently continuing with an obsession with the association between executives and shareholders, which believes that there is one right reply.

2.3 Determinants of Financial Performance of Commercial Banks

Financial performance is a target measure of an organization's general monetary wellbeing over a given time allotment and can besides be utilized to research comparative firms over a similar industry or consider organizations or sections in conglomeration. This study seeks to explore determinants of financial performance as follows:

2.3.1 Capital Structure

Capital structure alludes to the way in which an association is financed: a blend of long-term capital (ordinary shares and reserves, hybrid securities, convertible loan stock & bank advances etc.) and short-term liabilities, for example, a bank overdraft. A company's capital structure is then the composition or "structure" of its liabilities (Nirajini, 2013). Capital structure undertakes to determine the risk level of the association, and fixed cost is the key element whether it is incorporated into the production process or fixed financial expenses. The financing or capital structure decision is a critical administrative decision, as it influences the shareholder return and risk (Nirajini, 2013).

Higher level of debt is usually connected with better firm execution through the decrease of organization expenses and operational inefficiencies. The way a financial institution especially banks combines its debts and equity will define its performance. The achievement of commercial banks financial performance depends on efficient ways utilized to regulate the suitable amount of investment necessary to absorb unexpected misfortunes arising from the market credit and operational risk exposures (Myers, 2001).

Agency theory states that exclusion of top end administration and ownership adversely affects firm performance, as there is no impetus for administration to perform at maximum capacity. Debt is used as a mechanism to improve work ethics and performance of administration; nevertheless, an increase in the extent of debt compels the firm to experience higher financial distress (Jensen, 1986). In another view described by Wruck (1990), financial distress is more likely to cause commercial banks to experience bankruptcy; this alone inspires the administration to

improve firm execution, as they do not wish to endure job losses or bad repute because of bankruptcy as seen in the case of Imperial Bank Limited. The firm performance acts as depiction of operating profit as well as the relative market share.

2.3.2 Firm Size

The size of a firm influences performance from multiple points of view. Key elements of a large firm are its diverse capacities to exploit economies of scale and scope and the formalization of methods. These qualities, by making the execution of operations more successful, permit larger firms to produce better performance relative than smaller firms (Amato & Wilder, 1990). The number of employees is one of the standard measures of firm size (Konrad & Mangel, 2000). Economic theory prescribes that expanding firm size takes into consideration incremental progressive conditions since the size of the firm empowers it to raise the barriers of entry to prospective entrants and additionally gain influence on the economies of scale to achieve higher efficiency. For instance, on banking sectors area in Kenya, a new contender has little choice but to suffer fixed costs in gaining entry to the market, through acquiring and maintaining set capital requirements and investments in capital equipment to provide services to customers in addition to advertising extensively to alert customers of its existence in the market.

Amato and Amato (2004) demonstrate that the affirmative correlation between the size of the firm and productivity comes from realizing more conspicuous differentiation and specialization strategies, and should therefore prompt higher efficiency. Further researches likewise prescribe that bigger firms can exploit economies of scale. In this study, we focus our thoughts on firm size and evaluate its effect on firm profitability. Underlying hypothetical propositions contend that a firm

size recognized by its probability can be found in the obsolete points of view of the firm and the idea known as economies of scale. Economies of scale happen for various reasons. They can be: organizational reasons as far as division of labor and specialization skills; budgetary whereby a big firm can enhance its credit cost and get discounted rates on account of huge purchases; technical reason such as division of high fixed expenses over critical number of units and so on. In accordance with this idea, a positive association between firm size and benefit is normal.

Contrary to this, a theoretical framework that promotes an adverse relationship between firm size and profitability is noted in the alternate concepts of the firm such as Jermanis (2006), which suggests that large organizations are run by administrators looking after their own interests and subsequently, profit maximization as the company's objective capacity might be replaced by managers' utility maximization function.

2.3.3 Macroeconomic Variables

No firm can claim to be unaffected by what is happening on the international economic field given the expanded financial and economic integration that prevails today. Macroeconomic variables like interest rate, inflation rate and political risk have an impact on a firm's performance. The industry in which a corporation exists has a significant effect on its business performance. Porter (2008) contends that it is a key determinant of budgetary execution and its progressions may vary across industries. The impact delivered by the affirmation of a political threat for instance is frequently regarded in accounting as an extraordinary item. A few studies have demonstrated the issue in utilizing "phenomenal things" in this association as an instrument for the levelling out of income (Dempsey, Hunt & Schroeder, 1993).

Some studies suggest that the trend of Gross Domestic Product determines the demand for banks asset. During the weakening GDP growth, the demand for credit lessens thereby adversely influencing the profitability of banks. In contrast to that, in a developing economy as delineated by a favorable GDP growth, the interest for credit is higher because of the nature of business cycle. Amid the boom session, the interest for credit is high related to the depression period (Wainaina, 2013).

Academicians in the financial aspects field have offered an assortment of models for analyzing budgetary execution. Nevertheless, little assertions have risen on what constitutes a considerable arrangement of performance criteria (Tangen, 2003). Most studies completed by different researchers express that the effect of macrocosmic factors on the performance of banks shows a general rise in share prices, money supply, exchange rates, inflation and financing costs over certain periods. Kipngetich (2011) in his investigation of the relationship between financing costs and financial performance concluded that there is a positive relationship between financing costs and financial performance of commercial banks.

2.4 Empirical Literature

Robinson and Dechant (1997) revealed that diversity advances an unrivaled perception of the industry in which a firm works. Since the market itself is diverse, unique qualities will make it simpler for firms to penetrate these business segments. Robinson and Dechant (1997) comparably saw that diverse qualities in boards upgraded ingenuity and creative ability. This outlook in this way expresses the attitudes, convictions and intellectual working of people are not scattered in an arbitrary manner, all in all, to be methodically distributed with factors like race, sex and age. It is further perceived that diversity to the extent of gender prompts more

conspicuous critical thinking. This is because of various alternatives are meticulously assessed concerning advantages and disadvantages. A few researchers have contended argued that a board that is mixed as far as gender is concerned; is inclined to have an affirmative influence on its performance.

Erhardt, Werbel, and Shrader, (2003), did their study in the USA in a time period of six years starting from 1993 to 1998. The execution was measured by profit for resources and rate of return. Their exploration focused on vast organizations in each of the businesses in the USA. Notwithstanding the way that, the disclosures of this study were certain, it was trying to praise the confirmed results to the nearness of women administrators generally, as minorities are moreover joined. The minority could even be male business people who originated from minority tribes or gatherings. Distinctive experts have gone to a similar presumption that board contrasts have a certifiable result on firm execution.

Minguez-Vera and Campbell (2008) for instance, saw this to be the situation in Spain. Disregarding the way that firm execution was measured by Tobin's Q, the conclusion resembled those of bookkeeping measures like profit for resources and quantifiable profit. This evaluation did not concentrate all enterprises in Spain in that back segment firms were annulled from the specimen. This concentrate likewise tended to recorded in the financial segment of Madrid. Distinctive journalists, especially those from Australia have perceived that differing qualities is related to firm esteem in a positive way e.g. (Nguyen, 2011 (Bonn, 2004). Firm value was measured using Tobin's Q.

These studies included huge firms on the Australian stock trade for a time of two years from 2000 to 2001. They moreover connected 2 Stage Least Square (2SLS) strategy in its investigation of the impact of sexual orientation on firm execution. In as much as different investigates from different states have set up a positive result of board contrasts on firm execution, paying little respect to all that others set up an unfriendly impact. This shows how deficient concerning the thought of assorted qualities is. For example, (Bohren and Strom 2007) developed a negative relationship between board contrasts and firm execution for the Norwegian businesses. This is particular to various studies in the Scandinavian states which showed no relationship at all e.g. (Randoy et al. 2006).

Randoy et al. (2006) while undertaking a study in the Nordic nations of Denmark, Norway and Sweden saw that varying qualities in diverse boards don't have much effect on the running of the businesses. They surveyed execution by the entry in resources. Meanwhile, a study by (Rose, 2007) in Denmark set up relative results to those of Randoy et al. (2006) that board differing qualities makes little difference to firm execution. Rose's concentrate however revolved around recorded companies and used Tobin's Q as its execution measure as in opposition to Randoy et al. (2006) who used profits for resources. This concentrate likewise thought around nations as they were.

Regardless of the examinations of Randoy et al. (2006) and Rose, (2007) and Smith et al. (2006) identified that board sexual orientation assorted qualities decidedly influences execution of organizations in Denmark. Their study rotated around extensive 2500 Danish firms amidst the period 1993-2001. In any case, their study utilized execution techniques, for instance, net value added to net turnover, benefit on standard operations to net turnover, traditional result to net resources and net result

after duty to net resources which may be seen to be feeble. One thing that is normal among these investigates from Scandinavian countries is that they distinctly pushed on non-business firms.

In one study did in Ghana, Adusei (2010) discovered that board measure influences bank execution. He prescribed the way that littler sheets advantage the execution of the firm as assessed by profit for value. In an extra study on board measure, Staikouras et al. (2007) established that bigger banks distort the execution of banks in Europe. This along these lines demonstrates that the minor the board the higher the accomplishment of the bank. In as much as few studies have demonstrated that board measure influences execution, distinctive studies, for instance, those of Adams and Mehran (2005); Belkhir (2009), found no relationship between board size and firm execution. Specifically, Belkhir (2009) while undertaking a study on 174 US banks and speculation reserves associations did not express any positive relationship between board size and execution as measured by Tobin's Q.

Investigating board setup, Staikouras et al. (2007) found that board association does not affect firm execution regardless of the way that its relationship with execution was seen to be sure. These revelations resembled those of Adusei (2010) who found no association between board synthesis and bank execution in Ghana paying little heed to the way that board game plan was found to emphatically influence the result of bank suitability. In the time being, Alonso and Gonzalez (2006) thought on 66 banks in OECD nations from 1996 to 2003. They set up an adjusted U molded association between the measures of bank execution (Tobin's Q, ROA, the yearly market returns of a bank shareholder) and board estimate, which they speculate legitimizes a broad board yet authorizing a viable breaking point on size. Their disclosures likewise demonstrate a positive relationship between the non-official executives and execution.

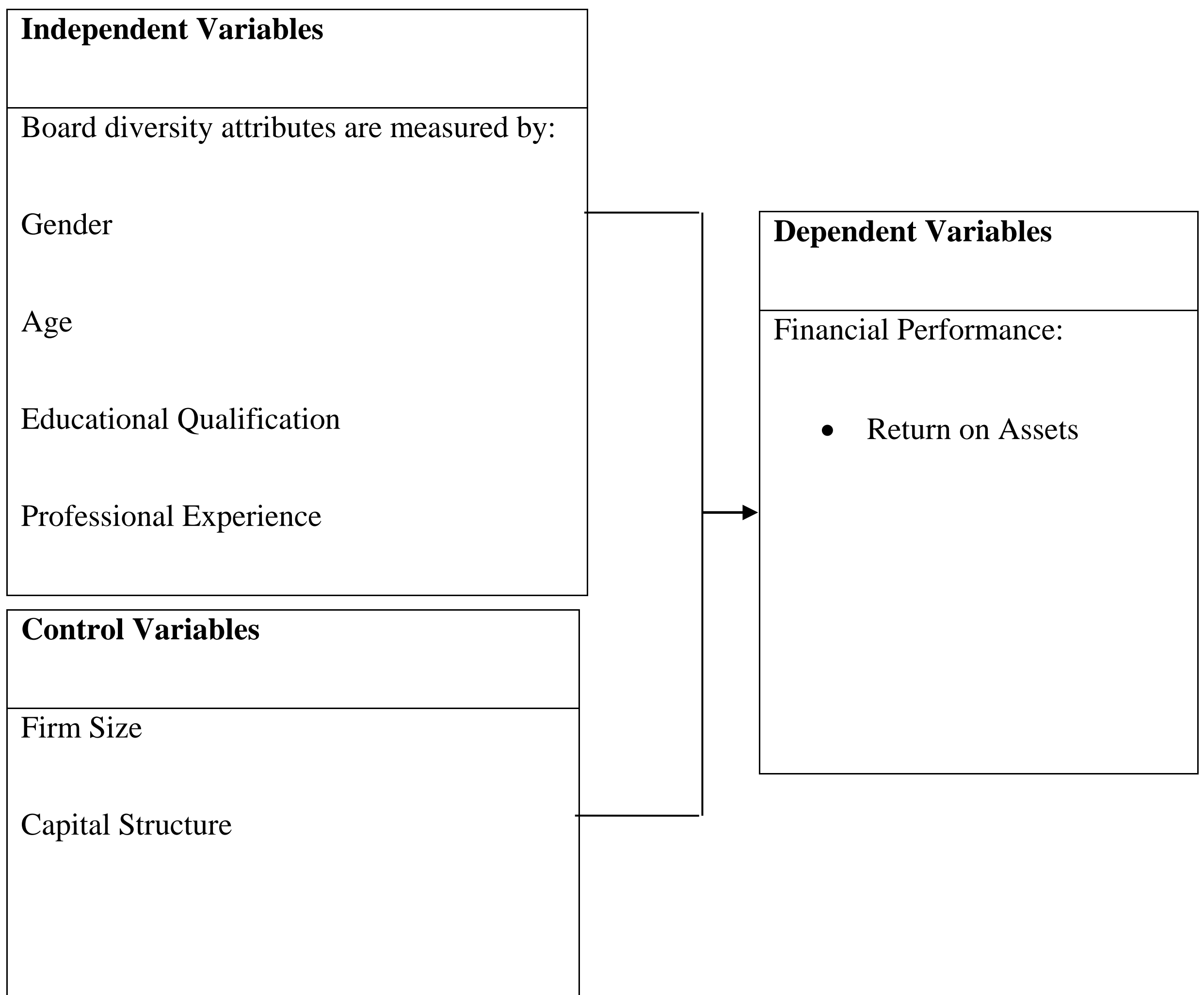
Busta (2007) attempted 69 recorded banks from the EU keeping cash range over the period 1996-2005 and 125 banks working in EU-15 and Switzerland amidst 2004. The disclosures for the 69 recorded banks reveal that a higher proximity of outside administrators on boards perform better correspondingly as the market to-book value and return for contributed capital, in Continental Europe, while unfriendly results were found by virtue of UK banks. Busta (2007) found no approval of an essential relationship between board sythesis and ROA. In the time being, the effect of the board size, but positive, was pointless in all cases. The results from the 125 banks show that board size has a certifiable association with the market to-book extent and degree of profitability and conversely related to return on resources; regardless it is insignificant a great part of the time.

Zulkafli and Samad (2007) assessed 107 banks in 9 Asian markets in 2004. Their discoveries suggest no basic relationship between execution measures (e.g. return on resources and Tobin's Q) and the board size or structure. At last, in perspective of a case of generally traded on an open market association on an open market US banks, Pi and Timme (1993) reported that cost capability and profit for resources are immaterial related to the rate of insider (outsider) officials.

Carter et al. (2003) led a study on the relationship between board differing qualities and firm execution with a unique thought on the operator speculation. The study uncovered that an expansion in the quantity of female chiefs may build the board's freedom. Assist, Smith et al. (2006), uncovered that board differing qualities enhances basic thinking as a pool of abilities and information rise from now on more decisions are assessed. Furthermore, a more differing board may similarly support an organization's favorable position gave it builds up the organizations picture and whether it decidedly influences customers' conduct and thusly on an association's execution (Smith et al., 2006).

2.5 Conceptual Framework

This conceptual framework gives a schematic relationship between the study variables. The study independent variable is board diversity, which is measured by gender age, education qualifications and personal experience. The dependent variable is performance, which is measured by return on assets. The control variable is firm size and capital structure.



2.6 Summary of Literature Review

Board arrangement incorporates the directors' capability to solve the different duties in the running of the organization (Daily, Johnson & Dalton, 1999) and has for the most part been investigated by looking at the demographic qualities of the board (Rindova, 1999). Board size and structure have for a long while been seen as basic segments of the administration system for firms' business as it depicts the partnership of each director as either inside or outside board member (Lawrence & Stapledon, 1999; Boone et al, 2007; Tricker, 2009). They take up an important role in the operations of the organizations.

Recent corporate reforms encourage women participation in corporate governance practices. The intention is to advance gender diversity in corporate boards. Corporations have been required to choose executives with diverse ethnic and gender backgrounds, expertise and age differences to their boards by institutional monetary investors, stockholder activists and vested parties (Van der Walt et al., 2006). The fundamental assumption is that more prominent differences ought to prompt less separate basic leadership forms and more noteworthy acknowledgment of progress (Westphal and Fredrickson, 2001; Bathula, 2008). This study therefore sought to fill the gap by investigating boards diversities and its effects on banks performance.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

This chapter indicates an impression of the techniques of data collection that was used; the methodology in which the data collection procedure followed and at the end tends to give the population that was used in the arriving of the conclusions thereof.

3.2 Research Design

This study considered causal research design since it endeavored to probe the effects of board diversity on financial performance of commercial banks in Kenya. Additionally, the study was explanatory in nature as it established whether the determinants including capital structure, firm size and macroeconomic variables caused banks performance to vary. The impact of board's diversity on bank financial performance was investigated over a five - year time span from 2010 to 2014. This period was selected with the goal that it would be easier and quicker to determine the real impact of boards diversity on financial performance execution; in any event for the boards where there could have happened these changes or arrangement and since a board has an existence range of six years, it will be then that the whole board be constituted or changed.

3.3 Population

The objective populace for this study was all the commercial banks in Kenya. These banks are forty-two (42) in number as per the Central Bank of Kenya's Banking Supervision Report of 2016. Each one of these banks was studied and an entire representative analysis was concluded.

3.4 Data Collection and Description

The pertinent information required for the study was collected mostly from secondary sources. The data pertaining to age, gender and education levels of the board members was collected from audited annual reports of the listed commercial banks. Information on financial performance was promptly accessible in secondary sources that incorporated financial information from financial statements of the commercial banks. These included the Nairobi Securities Exchange (NSE) annual publications, the NSE Handbook (2009) and the banks' annual reports and the Central Bank of Kenya website.

3.5 Data Analysis

Regression analysis was applied to form the association between the top managements' diversity and banks financial performance. Regression analysis was similarly used to evaluate the link between variables especially the level to which a dependent variable is a function of one or several independent variables (Hair et al., 1998; Saunders et al., 2007). Descriptive statistics were utilized to profile the board of directors of the target banks. Regression model was used to analyze the quantitative data and develop a predictor model for the study.

Ordinary Least Square (OLS) Random-Effects models was applied to test the hypotheses due to the important assumptions of homoscedasticity and no serial correlation in pooled data. An OLS regression was suitable since it adjusts for precluded variable bias, and proximity of auto-correlation and heteroscedasticity in pooled time arrangement information. This procedure permitted researchers to look at variations among cross-sectional units simultaneously with varieties within individual units after some time (Bathula, 2008). It is expected that relapse parameters won't

change after some time and won't vary between different cross-sectional units, upgrading the unwavering quality of the coefficient estimates. A critical presumption for choosing random effect is that the in secret heterogeneity won't be connected with the independent variables. Before playing out the regression analyses, the variables were tried for multi-collinearity following the technique in Hair et al., (1998). The method was appropriate for the study because it had one independent variable (board diversity attributes) and one dependent variable (financial performance).

According to the methods used and proposed above, this study created a regression model for implementing the empirical analysis.

Model : Financial Performance (Y) = $\alpha_0 + \beta_1 x_1 + \beta_2 x_2 + \beta_3 x_3 + \beta_4 x_4 + \beta_5 x_5 + e_{it}$

Y = measured by the Return on Assets (ROA) that's computed by net income divided by book value of total assets.

e_{it} = random error term

X_1 = age of the directors

X_2 = average period of experience

X_3 = gender of board members

X_4= education level of the board members.

β_1, β_2, β_3, $\beta 4$, β_5 = the coefficients for the independent variables.

α_0 = represents the intercept for X variable of the organization.

3.6. Test of Significance

The test of significance measured the possibility that the relationship between the variables stated in the regression model above exist and on the off chance that it does exist, how strong is the relationship.

As a measure of the strength of the relationship between the variables, an alpha value $\alpha = 0.05$ was picked. Also, P-value is the probability of finding the empirical sample results or higher results when the null hypothesis is true. The P- value was set at 0.05 i.e. $P \leq 0.05$.

CHAPTER FOUR

DATA ANALYSIS, INTERPRETATIONS AND PRESENTATION

4.1. Introduction

This chapter presents the data analysis on effects of board diversity on financial performance of commercial banks in Kenya. The study used descriptive and inferential statistics to analyze the findings. Descriptive statistics used mean and standard deviation to present the study outcomes. For inferential statistics, Pearson correlation, regression analysis and the t-test statistics were used.

4.2 Descriptive Statistics

The study analyzed the banks financial performance as measured by the return on assets proportion It also analyzed corporate board dynamics variables of interest namely; age of the directors, average period of experience, gender and education level. The variables mean, minimum and maximum and standard deviation is presented as shown in table 4.1

Variables	N	Minimum	Maximum	Mean	Std. Deviation
Return on Assets	5	0.01	0.21	0.0402	0.07089
Age of the Directors	5	45.00	57.00	52.4000	5.17687
Period of Experience	5	10.00	16.00	12.8000	2.38747
Gender	5	8.00	15.00	12.4000	0.03733
Education Level	5	3.00	4.00	3.6000	0.54772
Valid N (listwise)	5				

From table 4.1 the average return on assets for the commercial banks in Kenya is 4.02%. The average age of commercial banks directors is 52 years with a standard deviation of 5.17. Further the average years of experience as a board member is 12 years while the average representation of women in the boards of commercial banks in Kenya is 12.4%. On education level, the average education level for the banks board of directors is 3.6 which is an indication that majority of board members are university graduates.

4.3 Correlation Analysis

Table 4.1:Correlation Table

Correlation		Return on Assets	Age of the Directors	Period of Experience	Gender	Education Level
Return on Assets	Pearson Correlation	1	.502	.692	.731	.576
	Sig. (2-tailed)		.003	.0019	.000	.0010
	N	5	5	5	5	5
Age of the Directors	Pearson Correlation	.502	1	.918*	.804	.952*
	Sig. (2-tailed)	.003		.028	.101	.012
	N	5	5	5	5	5
Period of Experience	Pearson Correlation	.692	.918*	1	.711	.879*
	Sig. (2-tailed)	.0019	.028		.179	.049
	N	5	5	5	5	5
Gender	Pearson Correlation	.731	.804	.711	1	.882*
	Sig. (2-tailed)	.000	.101	.179		.048
	N	5	5	5	5	5
Education Level	Pearson Correlation	.576	.952*	.879*	.882*	1
	Sig. (2-tailed)	.0010	.012	.049	.048	
	N	5	5	5	5	5

As indicated in the table 4.2 above, there was a moderate positive correlation between return on assets and age of directors (0.502), period of experience (0.692), gender (0.731) and education level (0.576). This indicates that an increase in the study variables increase in firm's performance which would translate into a rise in return on assets. The above results show little evidence on multi co-linearity among the independent variable since the correlations among them are not very strong henceforth all can be used into consequent regression analysis

4.4 Regression Analysis

This section presents the outcomes of the combined effects of all the autonomous variables, which are age of the directors, average period of experience, gender and education level on the dependent variable that is Return on assets. A linear regression model was used to test the significance of the impact of the independent variables on the dependent variable. Therefore, the overall model for the study was; $Y_1=\alpha_0 + \alpha_1X_1+ \alpha_2X_2+ \alpha_3X_3+ \alpha_4X_4$

Table 4.2: Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.773[a]	.559	.523	1.62288

From the findings, the estimation of adjusted R squared was 0.523 a sign that there was variation of 0.523 on return on assets of commercial banks in Kenya due to deviations in age of the directors, average period of experience, gender and education level at 95% confidence interval. This demonstrates that 52.3% changes on return on assets by commercial banks in Kenya could be accounted for by changes in age of the directors, average period of experience, gender and education level. This shows that

47.7% change in return on assets in commercial banks is accounted by other factors other than age of the directors, average period of experience, gender and education level.

Table 4.3: ANOVA

Model	Sum of Squares	Df	Mean Square	F	Sig.
Regression	1.085	1	1.085	5.46912	.002[b]
Residual	17.802	3	5.934		
Total	**18.887**	**4**			

From the ANOVA measurements, the study proved the regression model had a significance level of 0.002 which is means that the information was ideal for making a conclusion on the population parameters. The computed value was greater than the critical value (5.46>1.96) a sign that directors age, average period of experience, gender and education level affect the commercial banks performance. The significance value was less than 0.05 indicating that the combined relationship between the selected factors on the return on assets of commercial banks was significant.

Table 4.4: Coefficients Table

	Unstandardized Coefficients		**Standardized Coefficients**	**t**	**Sig.**
	B	**Std. Error**	**Beta**		
(Constant)	14.527	3.747		3.87697	0.2
Age of Directors	0.174	0.011	0.139	15.8182	0.002
Period of experience	0.552	0.199	0.431	2.77387	0.004
Gender	0.087	0.041	0.002	2.12195	0.001
Education level	0.777	0.254	0.381	3.05906	0.003

Assuming a linear relationship between the independent and the dependent variable and guided by OLS estimation methods, the relationship between the independent and dependent variables as shown by the regression model was tested. The multiple regression equation was;

$Y = 14.527 + 0.174 X_1 + 0.552X_2 + 0.087X_3 + 0.777X_4$

From the above regression equation, it was discovered that holding executives age, average period of experience, gender and education level to a constant zero, financial performance would be at 14.527. A unit increment in the directors age would prompt an increment in financial performance of commercial banks by 0.174, a unit increment in as far as director's experience would prompt an increment in financial performance of commercial banks by 0.552, a unit increment in gender composition would prompt an increment in financial performance of commercial banks by 0.087 and unit rise in executives' education level would lead to an increase in financial performance of commercial banks by 0.777. All the four factors were found to significantly affect financial performance.

4.5 Discussion of the Findings

This study tried to examine the impact of board diversity on financial performance of commercial banks in Kenya. This paper assumed a survey of all the 42 commercial banks in Kenya whereby data was collected and analyzed for the years 2010 to 2014. Return on Assets(ROA) was used as the measure of financial performance. The study revealed that the average return on assets for the commercial banks in Kenya was 4.02%. Further the average age of commercial banks directors was 52 years with a standard deviation of 5.17. The normal years of experience of a board member was 12 years while the average representation of women in the boards of commercial banks

in Kenya was 12.4%. The correlation analysis revealed that there was a moderate positive connection between return on assets and age of directors (0.502), period of experience (0.692), gender (0.731) and education level (0.576).

This study further revealed that 52.3% changes on return on assets by commercial banks in Kenya could be accounted for by changes in age of the directors, average period of experience, gender and education level. The study also revealed that a unit increment in executives age would lead to prompt an increment in financial execution of commercial banks by 0.174, a unit increment in director's experience would prompt an increment in financial execution of commercial banks by 0.552, a unit increment in gender composition would prompt an increment in financial execution of commercial banks by 0.087 and unit increment in executives' education level would prompt an increment in financial execution of commercial banks by 0.777.

This study concurred with the academics of the stewardship theory who revealed that that executive-dominated boards should be preferred for their profundity of administration knowledge, access to recent working information, specialized skill and obligation to the firm (Letting' et al., 2012; Muth & Donaldson, 1998). The findings also go in line with those of Robinson and Dechant (1997) who likewise noticed that diversity in boards build innovativeness and creativity. It is revealed that diversity particularly as far as gender prompts more prominent critical thinking.

CHAPTER FIVE

SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1 Introduction

This study investigated the effects of board diversity on financial performance of commercial banks in Kenya. The study conclusions demonstrate statistically substantial positive relationship exists between financial performance (ROA) and executives' age, average period of experience, gender and education level.

5.2 Summary

This study clearly proved to be that directors' age, average period of experience, gender and education level has a positive relationship with the banks financial performance. The study conclusions make is it clear that diversity is a fundamental corporate governance element in the banking sector. A lot needs to be done to enhance individuals selected as directors in terms of their age, average period of experience; gender and education level may positively affect the performance of commercial banks.

The study found that firm performance based on the return on assets in the overall regression model is significant. This means that the independent variables of age, average period of experience, gender and education level are important forecasters of bank financial performance. Besides, it is acknowledged that board diversity and firm financial performances are interconnected (Dalton, 1999). The study also revealed a positive correlation between all the four variables and banks financial performance.

This means that as the board membership increase so does the female board members; this appears to contradict a study conducted by Ekadah and Mboya (2012) which found a negative relationship. The average female board member membership in Kenyan commercial banks was found to be 1 within the five years studied. Largely, more female representation on boards not only expands the size of the human capital pool from which the executives can be drawn, additionally gives a myriad of skills and knowledge that may not be plausible with all male in the banking boards. This finding is concurring with those of Wetukha (2013) who found an average gender representation of 1%, which was positively correlated to the financial performance of listed firms in Kenya's Nairobi Securities Exchange. According to the study findings the selected corporate board dynamics investigated namely; board size, board composition and gender diversity although found to be 41 significant predictors of banks financial performance they only explain 15% of the overall banks financial performance.

5.3 Conclusions

Directors' age, average period of experience, gender and education level has significant positive impact on the commercial banks financial performance. Large commercial usually have large size boards whereas smaller banks tend to have smaller boards. The study also concludes that there is a gender issue in the board composition in many banks.

Few women in the commercial banks board may have succeeded because women in most cases lack the required job training and work experience to govern the monetary sector. A study done in UK, noted that the number of female directors in finance, utilities and transport sector was a little bit higher when compared to other industries

(Grosvold, 2007). The study conclusions on the number of women executives on the Kenyan boards could also point to the fact that there is an unfair representation on women in numerous companies' boards.

5.4 Recommendations

On the premise of these study findings, the subsequent recommendations are being made; Commercial Banks should have a suitable and diverse board size designed so as to guarantee diversity of experience without conceding independence, accountability, compatibility, more knowledge, integrity and enthusiasm of members to attend meetings. The board size ought not to be excessively vast and ought to be comprised of qualified experts who are familiar with the oversight function.

Commercial banks should also attempt to incorporate more women members as it was proved to translate to more returns in terms of bank financial performance. It's therefore important that the right mix of both genders to be put in place in order to enhance excellent performance in the Commercial Banks in Kenya.

The number of non-executive and independent directors needs to be selected with a lot care since they affect financial performance commercial banks. The board needs to consist of well-educated and experienced professionals since they are actively involved in modeling the decisions of financial institutions.

Last but not least, commercial banks who value return on assets should have their board members serving for a shorter term and have more board members experienced in banking. Banks focusing on improving return on assets should reduce the board size and increase the ratio of female members in the board. Therefore, code for corporate governance should focus critically on these board dynamics as the keystone to achieving the much-needed financial performance in the commercial banks.

5.5 Limitations

This study faced that challenge of getting 100% of the required data from, 2010 to 2014. Most board and financial information for the five years 2010, 2011, 2012, 2013 and 2014 for some Banks was not available in the published accounts as well as the Central Bank of Kenya website. Some of the data that was presented in the annual financial reports had inconsistent figures in terms of age of the directors, professional experience and their level of education. Finally, there was a short timeline in conducting the research since it was survey involving all commercial banks in Kenya.

5.6 Suggestions for Further Research

This study investigated the impacts of board diversity on financial performance of commercial banks in Kenya. It may be valuable to progress this further utilizing other market based performance factors, for instance, Tobin's Q and compare the relationship. It may also be valuable if the study was carried out in the other sectors in the economy such as the insurance and manufacturing sector so as to come up with a conclusive position on whether board diversity variables do affect the performance of firms.

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APPENDICES

Appendix I: List of Banks

1. African Banking Corporation Limited
2. Bank of Africa Kenya Limited
3. Bank of Baroda (K) Limited
4. Bank of India
5. Barclays Bank of Kenya Limited
6. CfC Stanbic Bank Limited
7. Charterhouse Bank Limited- Under Statutory Management
8. Chase Bank (K) Limited- In Receivership
9. Citibank N.A Kenya
10. Commercial Bank of Africa Limited
11. Consolidated Bank of Kenya Limited
12. Co-op Bank of Kenya Limited
13. Credit Bank Limited
14. Development Bank of Kenya Limited
15. Diamond Trust Bank Kenya Limited
16. Ecobank Kenya Limited
17. Equatorial Commercial Bank Limited
18. Equity Bank Kenya Limited
19. Family Bank Limited
20. Fidelity Commercial Bank Limited
21. First Community Bank Limited
22. Guaranty Trust Bank (K) Ltd
23. Giro Commercial Bank Limited
24. Guardian Bank Limited
25. Gulf African Bank Limited
26. Habib Bank A.G Zurich
27. Habib Bank Limited

28. Imperial Bank Limited- In Receivership
29. I & M Bank Limited
30. Jamii Bora Bank Limited
31. KCB Bank Kenya Limited
32. Middle East Bank (K) Limited
33. National Bank of Kenya Limited
34. NIC Bank Limited
35. Oriental Commercial Bank Limited
36. Paramount Bank Limited
37. Prime Bank Limited
38. Sidian Bank Limited
39. Standard Chartered Bank Kenya Limited
40. Trans-National Bank Limited
41. UBA Kenya Bank Limited
42. Victoria Commercial Bank Limited

Appendix II: Education Levels

1	O-Level or KCSE certificate
2	Diploma
3	University graduate
4	University graduate-Masters Level
5	University graduate- PhD

Appendix III: Commercial Banks Data

Commercial Banks Combined Data	2010	2011	2012	2013	2014
Return on Assets	0.03	0.01	0.021	0.07	0.12
Age of The Directors	45	56	49	55	57
Director Experience	10	13	11	14	16
Gender	11%	13%	8%	15%	13%
Education Level	3	4	3	4	4
Size of The Firm (In Billions)	14,858	15,257	15,867	15,902	16,343