



**Strathmore**  
UNIVERSITY

Strathmore University  
**SU+ @ Strathmore**  
University Library

---

**Electronic Theses and Dissertations**

---

2015

An exploratory study of the relationship between corporate governance mechanisms and firm performance in Kenyan stockbrokerage firms

*Kamau, Florence Muchunu*  
*Strathmore Business School*  
*Strathmore University*

Follow this and additional works at: <https://su-plus.strathmore.edu/handle/11071/2474>

---

Recommended Citation

Kamau, F. M. (2015). *An exploratory study of the relationship between corporate governance mechanisms and firm performance in Kenyan stockbrokerage firms* (Thesis). Strathmore University. Retrieved from <http://su-plus.strathmore.edu/handle/11071/4719>

This Thesis - Open Access is brought to you for free and open access by DSpace @ Strathmore University. It has been accepted for inclusion in Electronic Theses and Dissertations by an authorized administrator of DSpace @ Strathmore University. For more information, please contact [librarian@strathmore.edu](mailto:librarian@strathmore.edu)

**AN EXPLORATORY STUDY OF THE RELATIONSHIP BETWEEN CORPORATE  
GOVERNANCE MECHANISMS AND FIRM PERFORMANCE IN KENYAN  
STOCKBROKERAGE FIRMS**

**Florence Muchunu Kamau**

**Submitted in partial fulfillment of the requirements for the Degree of Master of Business  
Administration at Strathmore University**



**School of Business**

**Strathmore University**

**Nairobi, Kenya**

**September 2015**

## Declaration

I declare that this work has not been previously submitted and approved for the award of a degree by this or any other University. To the best of my knowledge and belief, the thesis contains no material previously published or written by another person except where due reference is made in the thesis itself.

Florence Kamau

..... [Signature]

..... [Date]



## Abstract

The application of corporate governance in capital markets intermediaries' firms is aimed at ensuring stability and profitability of these firms. Stockbrokers in particular are expected to operate on the pillars of honesty, prudence and integrity and therefore the need to apply corporate governance mechanisms. The Capital Markets Authority (CMA) is the only body mandated to regulate Stockbrokers in Kenya. In order to strengthen governance and safeguard public interests in the capital markets industry, the CMA introduced the *CMA 2011 guidelines* on corporate governance. The rationale of this study was to investigate the corporate governance mechanisms and determine their effects on firm performance among the Kenyan stockbrokerage firms.

The specific objectives of the study were to establish the corporate governance mechanisms and practices relevant to the Kenyan stockbrokerage firms, to determine whether there is a relationship between corporate governance mechanisms and firm performance, identify the challenges in implementing the corporate governance mechanisms and to assess the extent of implementation of the CMA regulation on Corporate Governance.

The research design was exploratory and quantitative methods were used. The target populations were all the nineteen stockbrokerage firms listed and licensed in Kenya by the CMA and the main instrument was the questionnaire. Descriptive tables for mean, standard deviation, kurtosis and frequencies were then drawn and linear regression used to determine the relationship between the corporate governance mechanisms and firm performance (turnover). The forecasting model for performance of Kenyan stockbrokerage firms, was moderately significant with  $R^2$  of 48.3%.

The study concluded that the board and the audit committees are instrumental in managing the businesses in a professional manner. The study concluded that the extent of the implementation was mainly driven by regulatory requirement to comply with the guidelines as opposed to business objective. It is recommended that future studies include other dependent variables such as return on investments, net profit, shareholders value, quality of products/service, market share and customer satisfaction.

## Table of Contents

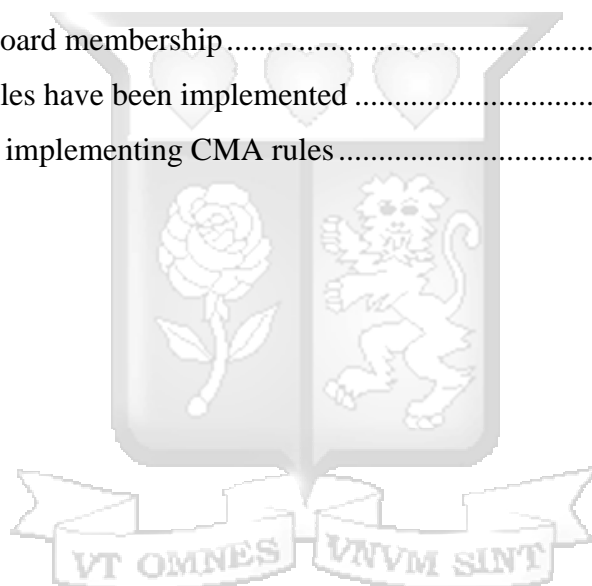
Declaration.....	ii
Abstract.....	iii
Table of Contents.....	iv
List of Figures.....	vi
List of Tables.....	vii
List of Abbreviations.....	viii
Acknowledgement.....	ix
CHAPTER ONE: INTRODUCTION.....	1
1.1 Background of the Study.....	1
1.2 Problem Statement.....	2
1.3 Research Objectives.....	4
1.4 Research Questions.....	4
1.5 Scope of the Study.....	5
1.6 Importance of the Study.....	5
1.7 Summary.....	6
CHAPTER TWO: LITERATURE REVIEW.....	7
2.1 Introduction.....	7
2.2 Concepts of Corporate Governance.....	7
2.3 Theories of Corporate Governance.....	10
2.3.1 The Stewardship Theory.....	10
2.3.2 The Social Entity Theory.....	11
2.3.3 Agency Theory.....	11
2.4 Theoretical Framework.....	13
2.5 Empirical Review.....	15
2.5.1 Empirical Studies Linked to the Study.....	15
2.6 Conceptual Framework.....	17
2.7 Research Hypothesis.....	17
2.8 Summary.....	18
CHAPTER THREE: RESEARCH METHODOLOGY.....	19
3.1 Introduction.....	19
3.2 Research Design.....	19

3.3	Target Population.....	19
3.4	Sample and Sampling Method.....	20
3.5	Data Collection.....	22
3.6	Pilot Test.....	22
3.7	Validity.....	22
3.8	Reliability.....	23
3.9	Data Analysis.....	23
3.9.1	Linear Model specification.....	24
3.10	Summary.....	24
<b>CHAPTER FOUR: PRESENTATION OF RESEARCH FINDINGS.....</b>		<b>25</b>
4.1	Introduction.....	25
4.2	Response Rate.....	25
4.3	Demographic Profile.....	25
4.4	Extent of Implementation of CMA Regulation on Corporate Governance.....	30
4.4.1	The Board.....	30
4.4.2	Audit Committee.....	34
4.4.3	Code of Conduct.....	36
4.5	Challenges in implementing CG mechanisms.....	37
4.6	Relationship between CG mechanisms and Firm Performance.....	38
<b>CHAPTER FIVE: DISCUSSION.....</b>		<b>41</b>
5.1	Introduction.....	41
5.2	The extent of implementation of CMA regulation on Corporate Governance in stockbrokers firms... 41	41
5.3	The challenges in implementing corporate governance mechanisms and practices among the Kenyan stockbrokerage firms.....	43
5.4	Relationship between Corporate Governance Mechanisms and Firm Performance among the Stockbrokerage Firms in Kenya.....	43
<b>CHAPTER SIX: CONCLUSION AND RECOMMENDATIONS.....</b>		<b>45</b>
6.1	Conclusion.....	45
6.2	Recommendations.....	45
<b>REFERENCES.....</b>		<b>47</b>
<b>APPENDICES.....</b>		<b>54</b>
Appendix A	- Timeline of Activities.....	54
Appendix B	- Letter of introduction.....	55
Appendix C	- Research Instrument.....	56

Appendix D	– List of Stockbrokerage firms in Kenya .....	62
------------	---	----

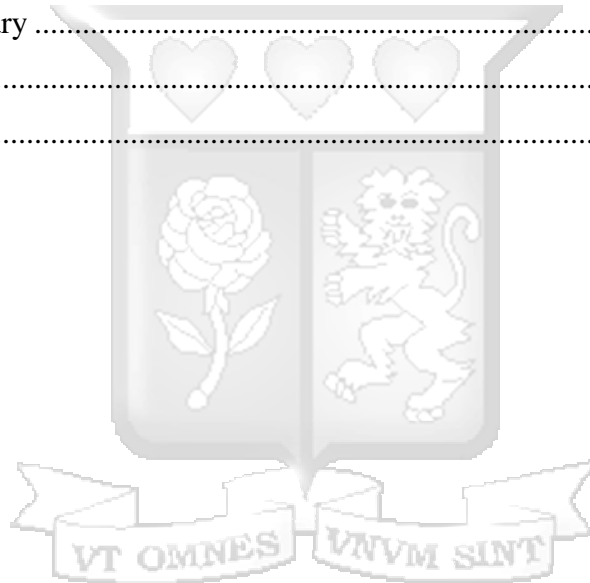
### List of Figures

Figure 2.1: Theoretical Framework .....	<b>Error! Bookmark not defined.</b>
Figure 4.1: Aggregate Firm Performance (Annual Turnover) of Stockbrokerage firms .....	26
Figure 4.2: Level of education .....	28
Figure 4.3: Length of operation .....	29
Figure 4.4: Ownership .....	29
Figure 4.5: Operation outside Kenya .....	30
Figure 4.6: Number of board members.....	31
Figure 4.7: Appointment of board members.....	32
Figure 4.8: Diversity of board membership.....	32
Figure 4.8: How CMA rules have been implemented .....	37
Figure 4.9: Challenges in implementing CMA rules.....	37



## List of Tables

Table 3.1: Sample Size .....	21
Table 4.1: Response Rate.....	25
Table 4.2: Firm Performance (Annual Turnover) of Stockbrokerage firms (2009-2012).....	27
Table 4.3: Summary of mean and standard deviation - the Board.....	33
Table 4.4: Summary of mean and standard deviation - audit committee .....	34
Table 4.5: Importance to factors affecting CG practices .....	35
Table 4.6: Elements of conformance and compliance - audit committee.....	36
Table 4.7: Summary of mean and standard deviation - code of conduct.....	36
Table 4.8: Coefficient Correlations.....	38
Table 4.9: Model Summary .....	38
Table 4.10: ANOVAb.....	39
Table 4.11: Coefficients.....	39



## Acronyms

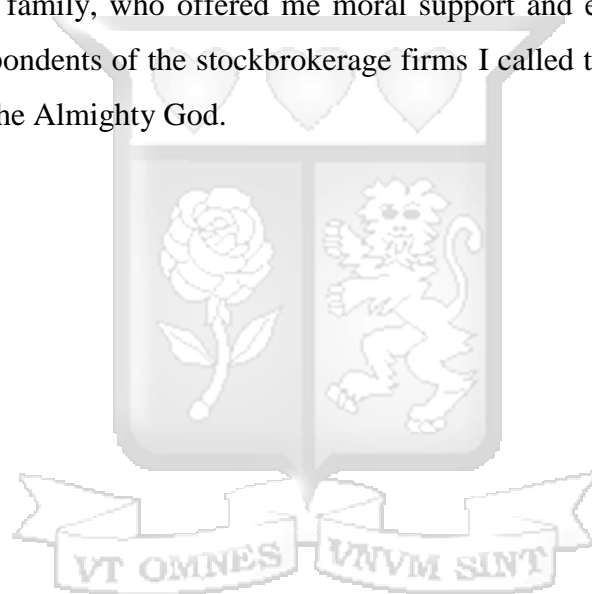
<b>CBD</b>	-	Central Business District
<b>CBK</b>	-	Central Bank of Kenya
<b>CDSC</b>	-	Central Depository & Settlement Corporation
<b>CG</b>	-	Corporate Governance
<b>CMA</b>	-	Capital Markets Authority
<b>FTSE</b>	-	Financial Times Stock Exchange
<b>GDP</b>	-	Gross Domestic Product
<b>IPO</b>	-	Initial Public Offering
<b>KRA</b>	-	Kenya Revenue Authority
<b>NSE</b>	-	Nairobi Securities Exchange
<b>OECD</b>	-	Organization for Economic Cooperation and Development
<b>PEV</b>	-	Post Election Violence
<b>SPSS</b>	-	Statistical Package for Social Sciences



## Acknowledgements

I wish to extend my sincere appreciation to Strathmore University for granting me the opportunity to further my education. My sincere appreciation goes to my supervisor, Dr. Elizabeth Muthuma, who guided me throughout the research process, with the much needed insights and encouragement. My heartfelt appreciation also goes out to the fraternity of Strathmore University, my classmates and support staff at the institution who in one way or the other extended their support.

I wish to also thank my family, who offered me moral support and encouragement. A special gratitude goes to the respondents of the stockbrokerage firms I called to ask for information and help. Above all, I thank the Almighty God.



## CHAPTER ONE: INTRODUCTION

### 1.1 Background of the Study

The Kenyan capital market has grown and become more active in mobilizing capital for prospective corporations wanting to list at the Nairobi Securities Exchange (NSE) as well as facilitating investment opportunities for the general investing public over the last ten years. Adrian (2009) suggested that corporate governance involves regulatory and market mechanisms and Ruppen (2002) defined it as the roles and relationships between a company's management, its board, its shareholders and other stakeholders, and the goals for which the corporation is governed. According to Carpenter & Westphal (2001), the board of a company consists of a team of individuals who combine their competencies and capabilities that collectively represent the pool of social capital for the firm which is contributed towards executing the governance function. The authors cited that the board should have significant proportions coming from inside directors to ensure more efficient and effective decision making.

O'Sullivan & O'Dwyer (2009) defined stock brokerage firms as financial institutions that facilitate the buying and selling of financial securities between a buyer and a seller and serve a clientele of investors who trade public stocks and other securities, usually through their firm's agent stockbrokers. In Kenya, the finance sector accounts for 12.3% of the GDP (AfDB, 2012).

Stock brokerage firms are licensees of the Capital Markets Authority (CMA) and as at the end of the year 2012, there were nineteen (19) licensed brokerage firms in Kenya (Appendix IV). These firms are a particular form of banking institutions which offer capital requirements of an enterprise through facilitating IPOs (Initial Public Offering), private placement and bond offerings as well as facilitating mergers and acquisitions of firms. Unlike the mainstream conventional banking institutions, investment banks are not allowed by CBK Act Cap 491 and the Banking Act 488 Laws of Kenya to accept deposits from customers.

In the management of stockbrokerage firms in Kenya, the regulator, CMA has come up with a number of corporate governance rules that will govern the management of these institutions. As per its guidelines on corporate governance practices, Capital Markets Regulations, 2011, (CMA,

2011), it is mandatory for any market intermediary operating in Kenya to establish a corporate governance framework that will provide strategic guidance of the organization and promote the effective monitoring of the management and accountability of the board. It is envisaged that by so doing, the organization will provide to the regulator and public, accurate information relating to its financial structure, ownership and governance. Further, the CMA regulations 2011 provide that the board shall review its corporate governance structure annually and the results of such review should be documented. In avoiding conflict of interest, CMA has also stipulated that the management of the market intermediary shall maintain adequate separation of employee duties particularly between those responsible for incurring commitment and those responsible for making payment as well as those responsible for preparing accounts.

Henry (2010) observed that there is a growing body of international evidence supporting the existence of a correlation between corporate governance structure, firm performance and valuation outcomes and hence the rationale of the study.

## **1.2 Problem Statement**

The CMA (2012) proposed amendments to Kenya's Capital Markets Authority CMA following the collapse of several Stockbrokers, loss of colossal amounts of money in the sector and some being put under statutory management. These stockbrokerage firms were Nyaga Stockbrokers, African Alliance, Kenya Investment Bank Limited, Faida Investment Bank Limited, Francis Thuo and Partners Limited, Ngenye Kariuki and Company Limited, Discounts Securities Limited and Genghis (CMA, 2012). The CMA cited poor corporate governance mechanisms hence need to determine the relationship between corporate governance mechanisms and firm performance.

The aim of this study was to investigate the corporate governance mechanisms and determine their effects on firm performance (measured in terms of turnover) among the Kenyan stockbrokerage firms. According to the CMA, the Kenyan capital market has been able to facilitate the raising of over Kshs 1 billion of capital a 10 year period. This growth took place in the earlier period with little or regulatory guidance through what can be termed as self regulation by the market participants. As a result of the inadequate regulation of the sector and wanting

internal structures governing the operations of these brokerage firms, the sector has witnessed several of these firms going under with millions of client's investment. As a result, several regulatory mechanisms such as raising the capital base from KES 50 million to KES 250 million and the publication of the twin regulations of Legal Notice No. 144 Capital Markets (Corporate governance) (Market Intermediaries) Regulations, 2011 and Legal notice no. 145 Capital Markets (Conduct of Business) (Market Intermediaries) Regulation, 2011 that deals with conduct of businesses came into force.

Prior to the said regulatory changes, four main stockbrokerage firms were put under statutory management by CMA following their inability to perform their stockbrokerage functions. These were, Francis Thuo & Partners Ltd, Nyaga Stockbrokers Ltd, Ngenye Kariuki & Company Ltd and Discounts Securities Ltd. These occurrences suggest a need to investigate the corporate governance mechanisms and determine their effects on turnover. Turnover as a measure of performance was used because the data for all the firms were readily available over the financial period 2009-2012. At the same time as compared to other quantitative performance measures, sales figures did not require further computations like ratios which made it easier to use. The structuring of the board, the audit committee and the implementation of the code of conduct in the management of stockbrokerage firms was aimed at curbing the excesses of owner/managers and thus scaling up the returns, improving efficiency and instilling professionalism (Strathmore, 2013).

The unfortunate events in the stockbrokerage fraternity have also drawn concerns from the Central Bank of Kenya. The Central Bank of Kenya (CBK, 2012) stated that with the unprecedented growth of the Kenyan financial markets in the recent past, new challenges have emerged which require concerted efforts of all players in order to safeguard the integrity of the stock market. The CBK (2012) cited that a number of stock exchange brokers have not been operating within the kind of corporate governance framework that would be expected of them. The interest of the CBK as the overseer of financial system in the country is mainly drawn from the fact failure in the capital markets can easily have a knock on effect on the entire financial system.

The Kenyan stockbrokerage sector is appropriate for conducting this research for several reasons. First, the failure of several local firms has highlighted the need for corporate governance (CG) reform in the sector. Secondly, in the last decade, there has been a rising interest in investing in Kenya and the East African countries, which has demonstrated a huge economic growth potential. The Kenyan stockbrokerage firms have organized both local and regional IPO for some of the major corporate firms and with the increased need for expansion in the region, most of these firms will continuously need additional funding which will be sourced from the public by these market intermediaries. Thirdly, Nairobi is an international financial center. However, most of the stock brokerage firms are family or partnership owned and their practice of corporate structure practices will be of interest to study.

Despite the importance of the managers of a firm practicing corporate governance principles in the running of business organizations, there have been limited studies done locally and none that the researcher is aware that has been done in the stock brokerage sector in Kenya.

### **1.3 Research Objectives**

From the background examined and the rationale of the study, the general objective of the study was to determine the influence of corporate governance mechanisms on the firm performance measured in terms of annual turnover. The specific objectives were;

- i. To assess the extent of implementation of CMA regulation on Corporate Governance in stockbrokerage firms
- ii. To identify the challenges in implementing corporate governance mechanisms and practices among the Kenyan stockbrokerage firms.
- iii. To determine whether there is a relationship between corporate governance mechanisms and firm performance among the stockbrokerage firms in Kenya

### **1.4 Research Questions**

From the background highlighted and research objectives formulated, the research questions were;

- i. What is the extent of the implementation of CMA regulation on Corporate Governance in stockbrokerage firms?
- ii. What are the challenges in implementing corporate governance mechanisms and practices among the Kenyan stockbrokerage firms?
- iii. What is the relationship between corporate governance mechanisms and firm performance among the stockbrokerage firms in Kenya?

### **1.5 Scope of the Study**

This research focused on the stockbrokerage firms in Kenya with their headquarters in Nairobi County. It was limited to those firms that have operated for the last five years in order to comprehensively investigate the relationship between the CMA mechanisms introduced in 2011 and the firm performance turnover.

### **1.6 Importance of the Study**

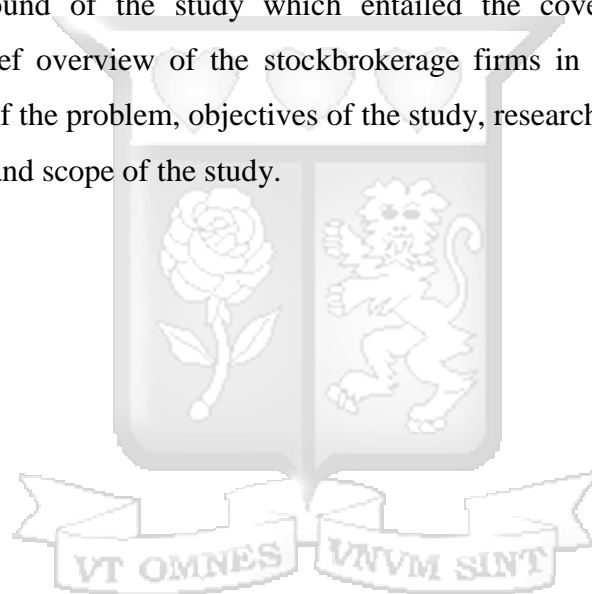
To policy makers and regulators, the understanding of the influence that corporate governance has on the performance of stockbrokerage firms will help policy makers – governments and other stakeholders – to design targeted policies and programs that will actively stimulate the growth and sustainability of the stockbrokerage firms in the country, as well as helping those policy makers to support, encourage, and promote the establishment of these firms. Regulatory bodies such as the Central Depository & Settlement Corporation (CDSC), the Capital Markets Authority (CMA), the Kenya Revenue Authority (KRA) and the Nairobi Securities Exchange (NSE) can use the study findings to improve on the framework for regulation and build investor confidence.

To the senior management of stockbrokerage firms in Kenya, the study will provide insight into how their firms can effectively develop and practice appropriate corporate governance. This study will offer an understanding on the importance of adopting appropriate corporate governance and postulating the relationship that exist between the existing corporate governance and their organizational performance.

The results of the study would also be important to academicians and scholars, to serve as a point of departure for further investigation into the relationship between governance practices and firm performance. There was need of understanding better how boards add value to companies by incorporating qualitative factors in the analysis. The results of the study will form part of the literature on corporate governance and particularly on the relationship between observance of corporate governance and firm performance.

## **1.7 Summary**

Chapter one expounded on the subject area of the research. The research aimed at determining the role of corporate governance on performance of brokerage firms in Kenya. The chapter highlighted the background of the study which entailed the coverage of what corporate governance is and a brief overview of the stockbrokerage firms in Kenya. The chapter also presented the statement of the problem, objectives of the study, research questions, importance of the study, the limitation and scope of the study.



## CHAPTER TWO: LITERATURE REVIEW

### 2.1 Introduction

Chapter two examined extant literature and from this, formulated a theoretical framework, to gain more understanding on the subject area. The Chapter examined the theoretical concepts of corporate governance among stock brokerage firms and empirical studies linked to the study in detail. In order to clarify the research area, a conceptual framework was formulated and hypotheses extracted as suggested by Trochim & William (2006). Within these subject areas, a number of authors were cited and acknowledged.

### 2.2 Concepts of Corporate Governance

The issue of corporate governance (CG) has become prominent in the recent past due to reported scandals in Europe and America. However, the issue of corporate governance has actually been in existence for ages (Vermeeren, 2006). As Ruppen (2002) acknowledged that CG is a combination of issues concerning the management, the supervision and relationship among top level institutions and the different stakeholders hence it is important for all forms of entities both public stock corporations as well as family owned companies. Petzold & Nippa (2005) concurred and observed that CG can be assumed to be mandatory in almost all forms of organizations.

According to Von Werder (2003), CG can be looked at from two perspectives. The internal that deals with rights, competencies and the interactions between the supervisory board and the board of directors and the external that focuses on the relationship between the corporation and the different stakeholders of the corporation. The basic essence of corporate governance is to make sure that the key shareholder objective of maximizing wealth is implemented by all those entrusted with the task of managing the affairs of the companies.

A typical board structure is composed of outside directors and top company officers. Outside directors are appointed by the company's shareholders and are assumed to be acting in the shareholders' interests. Top company officers possess critical information regarding current and future activities and operations, which are necessary for the decision-making process, performance evaluation, and monitoring (Lang and Jagtiani, 2010).

According to Ruppen (2002), the inclusion of top management among board members may give rise to a conflict of interest as management may attempt to transfer wealth from stockholders by taking advantage of information asymmetry and this is likely in a situation where the company ownership concentration is low and this might lead to top management and directors colluding. To mitigate against this potential agency problem, shareholders seek to structure a board that is able to guarantee an acceptable degree of independence.

With a robust board structure in a stockbrokerage firm, the risk of collusion with top management is reduced, as independent directors are expected to ensure that the law is respected and to limit agency problems (Fama & Jensen, 1983). The OECD (2004) stated that good corporate governance should provide proper incentives for the board and management to pursue objectives that are in the interests of the company and its shareholders and should facilitate effective monitoring. The presence of an effective CG system helps to provide a degree of confidence that is necessary for the proper functioning.

Lang & Jagtiani (2010) acknowledged that operational managers need to act in the interests of the owners of the entities and other stakeholders and sound corporate governance encourages the efficient use of resources and provides for accountability for the stewardship of those resources by managers. This means that in the context of the Kenyan stock brokerage firms it will be expected that the brokers as the agents of the potential investor will be expected to act to the best interest of the investor. If this is followed, then the broker will be expected to facilitate the buying and selling of the customer securities without using that position created from the relationship to unnecessarily benefit from the transaction or use the funds deposited for any other purposes outside what was intended for.

Stock brokerage firms that practice good corporate governance are more likely to achieve institutional objectives and goals and this implies that good corporate governance should be of prime concern to owners and other stakeholders of these institutions. In fact, good corporate governance helps promote the general welfare of the society and should be of interest to the general public and governments (Freidank, Velte & Weber 2009).

The OECD has been in the forefront in promoting CG in organizations because of its belief in the link between corporate governance and firm performance. OECD (2004) appraised the revised CG principles, meant to strengthen corporate governance around the world. The revised OECD principles on corporate governance focus on a number of areas that it encourages to be followed in an organization. These pertinent issues are related to the governance of a firm operation and aims at promoting transparent and efficient financial markets, protecting and facilitating of the exercise of shareholders' rights, equitable treatment of all shareholders including minority and foreign shareholders, recognizing the rights of other stakeholders; timely and accurate disclosure of all material matters; and strategic guidance of the firm by boards of directors, including board accountability to the firm and board effectiveness in monitoring management (OECD 2004).

The above tenets of corporate governance define important relationship that should exist between an investor and the broker in the brokerage sector and the general corporate scene in Kenya. CG is important for public stock corporations and other types of enterprises. It can be assumed that aspects of CG are almost relevant for all forms of organizations (Petzold & Nippa, 2005).

Corporations have become a powerful and dominant institution. They have reached to every corner of the globe in various sizes, capabilities and influences. Their governance has influenced economies and various aspects of social landscape. Shareholders are seen to be losing trust and market value has been tremendously affected. Moreover with the emergence of globalization, there is greater deterritorialization and less of governmental control, which results in a greater need for accountability (Crane and Matten, 2007). Hence, corporate governance has become an important factor in managing organizations in the current global and complex environment. In order to understand corporate governance, it is important to highlight its definition. Even though, there is no single accepted definition of corporate governance but it can be defined as a set of processes and structures for controlling and directing an organization. It constitutes a set of rules, which governs the relationships between management, shareholders and stakeholders.

## **2.3 Theories of Corporate Governance**

Corporate governance includes all types of firms and its definitions could extend to cover all of the economic and non-economic activities. Literatures in corporate governance provide some form of meaning on governance, but fall short in its precise meaning of governance. Such ambiguity emerges in words like control, regulate, manage, govern and governance. Owing to such ambiguity, there are many interpretations. It may be important to consider the influences a firm has or affected by in order to grasp a better understanding of governance. Owing to vast influential factors, proposed models of corporate governance can be flawed as each social scientist is forming their own scope and concerns. Hence, this dissertation reviews various fundamental theories underlining corporate governance. These theories range from the stewardship theory, social entity and agency theory.

### **2.3.1 The Stewardship Theory**

The Stewardship theory contends that if one person is both involved in the management of the firm as well as undertaking a supervisory function, this may improve firm performance since such structure removes any internal and external ambiguity regarding responsibility for the firm's processes and outcomes (Donaldson & Davis, 2004).

The stewardship theory claims that managers are good stewards of the corporation. Based on a traditional legal view of the corporation as a legal entity in which directors have a fiduciary duty to the shareholders, the stewardship theory argues that managers are actually behaving just like stewards to serve the shareholders' interests and diligently work to attain a high level of corporate profit and shareholder returns. Managers have a wide range of motives beyond a simple self-interest, such as achievement, recognition and responsibility needs, the intrinsic satisfaction and pleasure of successful performance, respect for authority, social status, and work ethics (Nicholas, 2009).

Thus, the separation of ownership from control does not inherently lead to a goal and interest conflict between shareholders and managers. The separation actually promotes the development of managerial profession, which is certainly beneficial for corporate performance and

shareholder wealth. In this regard, empowering managers to exercise unencumbered authority and responsibility is necessary for the maximization of corporate profits and shareholders' value (Etzioni, 2005).

### **2.3.2 The Social Entity Theory**

The social entity conception of the corporation regards the corporation not as a private association united by individual property rights, but as a public association constituted through political and legal processes and as a social entity for pursuing collective goals with public obligations (Gamble & Kelly, 2001). This perspective views the corporation as a political tool for social purposes (Dine, 2000,) and argues that individual property rights are conditioned and restrained in a social context and in community (Warren, 2000). The social entity theory views the corporation as a social institution in society based on the grounds of fundamental value and moral order of the community.

Sacks (1997) suggested that human attachments and affiliations, loyalties and likes are both moral and fundamental; they enter into the identity and understanding of specific persons and cannot be reduced to contractual alliances for the temporary pursuit of gain. With the fundamental value of human rights and morality as a reference framework, the standard of a corporation's usefulness is not whether it creates individual wealth but whether it helps society gain a greater sense of the meaning of community by honoring individual dignity and promoting overall welfare (Sullivan & Conlon, 1997).

Corporations are granted by the state not only as an economic entity for a commercial purpose, but more importantly, as a social entity for general community needs. The corporation has a collective, rather than individual identity and executives are representatives and guardians of all corporate stakeholders' interests (Hall, 1989).

### **2.3.3 Agency Theory**

The agency theory separates decision and risk bearing functions observed in large corporations (Fama & Jensen, 1983). The authors cited that the separation of decision and risk bearing

functions survives in these organizations not only because of the organizational structure but in part because of the benefits of specialization of management and risk bearing function that led to an effective common approach to controlling the agency problems caused by separation of decision and risk bearing functions. They posit that the contract structures of all these organizations separate the ratification and monitoring (control) of decisions from initiation and implementation (management) of the decisions.

Jensen & Meckling (1976) defined an agency relationship as a contract under which one or more persons (the principal(s)) engage another person (the agent) to perform some service on their behalf which involves delegating some decision making authority to the agent. They therefore argue that since the relationship between the stockholders and manager of a corporation fit the definition of a pure agency relationship it should be no surprise to discover that the issues associated with the “separation of ownership and control” in the modern diffuse ownership corporation are intimately associated with the general problem of agency. It is generally impossible for the principal or the agent at zero cost to ensure that the agent will make optimal decisions from the principal’s viewpoint and this therefore necessitates the incurrence of the agency costs. In most agency relationships the principal and the agent will incur positive monitoring and bonding costs (non-pecuniary as well as pecuniary), and out of these agency costs, they argue that there will be some congruence between the agent’s decisions and those decisions which would maximize the welfare of the principal.

According to Agrawal & Knoeber (1996), agency problems arise within a firm whenever managers have incentives to pursue their own interests at shareholder expense. Several mechanisms have been advanced to reduce the level of agency problems and these actions include managerial shareholdings, concentrated shareholdings by institutions or by block holders can increase managerial monitoring and so improve firm performance, as an outsider representation on corporate boards. In addition, the use of debt financing can improve performance by inducing monitoring by lenders. The labor market for managers can motivate managers to attend to their reputations among prospective employers and which will lead to improvement of performance. Finally, the threat of displacement imposed by the market for corporate control can create a powerful discipline on poorly performing managers.

## 2.4 Theoretical Framework

Other than the fundamental corporate governance theories of agency theory, stewardship theory and social entity theory to corporate governance, there are other ethical theories that can be closely associated to corporate governance like the business ethics theory. Business ethics is a study of business activities, decisions and situations where the right and wrongs are addressed. The main reasons for this are the power and influence of business in any given society is stronger than ever before.

Businesses have become a major provider to the society, in terms of jobs, products and services. Business collapse has a greater impact on society than ever before and the demands placed by the firm's stakeholders are more complex and challenging. Only a handful of business giants have had any formal education on business ethics but there seems to be more compromises these days.

Business ethics helps us to identify benefits and problems associated with ethical issues within the firm and business ethics is important as it gives us a new light into present and traditional view of ethics (Crane and Matten, 2007).

In understanding the 'right and wrongs' in business ethics, Crane & Matten, (2007) injected morality that is concerned with the norms, values and beliefs fixed in the social process which helps right and wrong for an individual or social community. Ethics is defined as the study of morality and the application of reason which sheds light on rules and principle, which is called ethical theories that ascertains the right and wrong for a situation.

In order to clarify and gain much more understanding of the subject area, the theoretical framework/model was formulated from the reviewed theories. The Theoretical framework is presented in Figure 2.1 next.

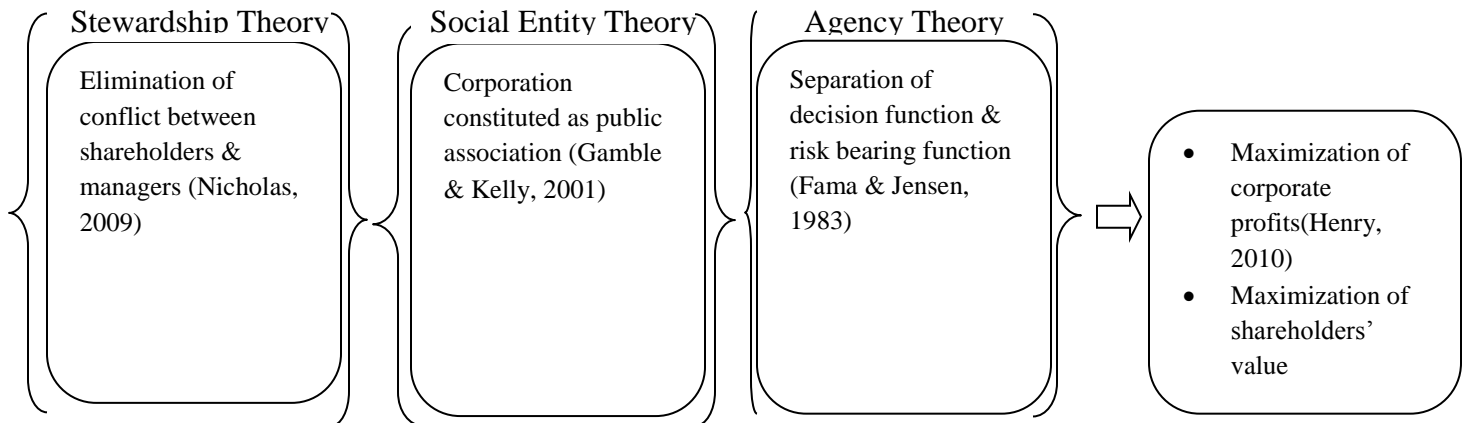


Figure 2.1: Theoretical Framework

From the authors examined and the theories examined, it can be deduced that for maximization of profits and shareholders' value in stockbrokerage firms, the most appropriate model of CG would involve having a Board, a Code of Conduct and Audit Committee functions. It has been argued that the board is ultimately responsible for the system of internal control (Dunne & Helliard, 2002) and that an effective system of control comprises of a solid environment, adequate risk assessment, specific control activities, segregation of duties, adequate information and communication processes and sufficient monitoring.

These activities are related to the three theories and thus there is a link between the board, code of conduct and audit committee and the 3 theories. The presence of a board following CG principles can be explained by the stewardship theory. Stewardship theory assumes that managers, in this case the board, are stewards whose behaviors are aligned with the objectives of their principals. The elimination of conflict between shareholders and managers (stewardship theory) translates into benefits of unity of direction and of strong command and control, and adequate information and communication processes. The presence of a code of conduct can be traced back to the having the corporation constituted as a public entity (social entity theory) which not only serves as an economic entity but as a social entity for general community needs. The audit committee's role is to assist the board discharge its oversight functions and manages the risk and the separation of decision function and risk bearing functions (agency theory).

## **2.5 Empirical Review**

### **2.5.1 Empirical Studies Linked to the Study**

The existence of a correlation between corporate governance structure, firm performance and valuation outcomes was studied by Henry (2010). What is less clear from this evidence, however, is the channel through which governance mechanisms derive their impact. Prior studies have suggested stronger shareholder rights and legal protection mechanisms which lower investor capital costs (La Porta et al. 2000) or incentive effects associated with takeover vulnerability (Bebchuk et al., 2009).

Other suggested channels include greater coverage and reporting by ratings agencies (Brown and Caylor, 2006), improved management structure and oversight through voluntary or legislative enforcement of codes of governance practice (Henry, 2008), and enhanced disclosure information (Beekes, Brown & Chin, 2006). These channels have not been exhaustively applied or tested in the Kenyan stockbrokerage firms. Furthermore, there is other work intimating that it may, in fact, be prior or contemporaneous performance or valuation outcomes that are driving changes in the corporate governance structure of firms (Hermalin & Weisbach, 2003)

In their study, Bassen & Zollner (2007) acknowledged that the reason that led to the closure of stockbrokerage firms in developed countries was the lack of proper governance structures that led to manipulations of balance sheets. The authors acknowledge the need of a mechanism to deal with the management and the supervisory system as well as the legal and factual regulation framework for the interaction of management, board and stakeholders. The Board composition, according to Bassen & Zollner (2007), was seen as playing an important role in facilitating effective mechanisms of running internal affairs of stockbrokerage firms.

Gompers, Ishii & Metrick. (2003) classified 24 governance factors into five groups (tactics for delaying hostile takeover, voting rights, director/officer protection, other takeover defenses, and state laws), and created G-Index by summing the 24 binary governance factors. They found that an investment strategy that bought firms in the lowest decile of the index (strongest rights) and sold firms in the highest decile of the index (weakest rights) would have earned abnormal returns of 8.5 percent per year during the sample period. Also, firms with stronger shareholder rights had

higher firm value, higher profits, higher sales growth, lower capital expenditures, and made fewer corporate acquisitions. Firms with fewer shareholder rights have lower firm valuations and lower stock returns. However, Gompers et al. (2003) caution the interpretation of their results by stating that since this is an experiment without random assignment, no analysis of causality can be conclusive. The main problem is the possibility that some unobservable characteristic is correlated with G and is also the main cause of abnormal returns.

Bauer, Guenster & Otten (2004) followed the approach of Gompers et al. (2003). Using data from Deminor Corporate Governance Ratings for companies included in the FTSE Euro top 300, portfolios were built consisting of well-governed and poorly governed companies and their performances compared. The impact of corporate governance on firm valuation was also examined. The results show a positive relationship between these variables and corporate governance. This relationship weakens substantially after adjusting for country differences. Finally, the relationship between corporate governance and firm performance as approximated by net profit margin and return on equity was analyzed. Surprisingly, and contrary to Gompers et al. (2003), a negative relationship is found between governance standards and earnings-based performance ratios.

Cremers & Nair (2005) followed Gompers et al. (2003), to study how these governance mechanisms interact with long-term equity prices. Using the classifications from the governance index that they developed, they showed that a portfolio that buys firms with the highest level of shareholder rights and sells firms with the lowest level of shareholder rights generates an annualized abnormal return of 8.5% from 1990 to 1999.

They further consider two different proxies for internal governance: the percentage share ownership by institutional block holders, defined to be an institutional shareholder with equity ownership greater than 5%, and the percentage of share ownership by public pension funds, which tend to be active shareholders. They find that public pension fund (block holders) ownership is important only in the presence of takeover vulnerability and that the market for corporate control is important only in the presence of an active shareholder—firms with the highest quartile of block holder (public pension fund) ownership.

Whereas Bhagat & Black (2002) find no relationship between the proportion of independent directors and various indicators of firm performance, Rosenstein & Wyatt (1990) observe a positive market reaction to the appointment of independent directors. Perry and Shivdasani (2005) explain that firms with a majority of outside directors are more likely to restructure following performance declines, and more determined in doing so. Dunlop (2000) explains that an executive Board should ensure that the agency is conforming to legislation and government policies and achieving agreed outcomes. A major issue in carrying out the Executive Board's conformance function is independence-whether board members who are likely to be also managers can sensibly be expected to report openly on what is effectively happening in organization (their own management performance), and be seen to be doing so by those to whom they are accountable.

## **2.6 Conceptual Framework**

Following the reviewed literature, the study proposed a conceptual framework in which the independent variable is Corporate Governance mechanisms (The board, audit committee and code of conduct) while Stockbrokerage firm performance (turnover) is the dependent variable.

It was postulated that the corporate governance mechanisms have a direct effect on the stockbrokerage firm performance. The OECD (2004) also related well documented CG mechanisms to firm performance and valuation outcomes and the CBK (2012) acknowledged the unprecedented growth of the Kenyan financial markets in the last 10 years from the year 1990. All these outcomes are geared towards firm performance and shareholders' value.

## **2.7 Research Hypothesis**

From the literature review examined, the conceptual framework was formulated and the following hypotheses formulated:

H<sub>1</sub>: There is a positive significant relationship between the role of the board and firm performance (turnover)

H<sub>2</sub>: There is a positive significant relationship between the role of audit committee and firm performance (turnover)

H<sub>3</sub>: There is a positive significant relationship between code of conduct and firm performance (turnover)

## **2.8 Summary**

Chapter two examined relevant literature review that pertained to the research questions. From theoretical review all authors generally, examined the concepts of CG, existent mechanisms, the board structure and role of management and board. In order to gain more in-depth understanding in the subject area, the theories of CG were reviewed. In the three theories, it could be summarized that the key issues were having a steward, constituting the stockbrokerage firms as a public entity and separating decision making functions from risk functions. From the empirical review, the authors generally concurred on an existence of a correlation between corporate governance structure with firm performance and valuation outcomes.

The conceptual framework was formulated and hypotheses extracted. This study now sought to collect data and accept or reject the hypotheses and answer the research questions.



## **CHAPTER THREE: RESEARCH METHODOLOGY**

### **3.1 Introduction**

This chapter described the research design and methodology that was employed in the study. It also justified the choice of methodology applied to conduct the research as well as highlighted details of the target population, sampling technique, instruments of data collection, data analysis, validity and reliability.

### **3.2 Research Design**

In order to accept or reject or fail to reject the formulated hypotheses, investigate the corporate governance mechanisms and determine their effects on firm performance among the Kenyan stockbrokerage firms, there was need to track the corporate profits and annual turnovers through a 3 to 5 year time period. Based on the nature of the study, the study used an exploratory research design as suggested by Winnie (2006) who advised that if there was need to generally draw conclusions, test a specific hypothesis or use random sampling techniques so as to infer from the sample, then the exploratory research design would be appropriate. The exploratory research design was also appropriate as it involves gathering data that describe events and then organizes, tabulates, depicts, and describes the data collection (Grace, 2005).

There was also a quantitative phase that collected numeric responses in order to investigate the corporate governance mechanisms and determine their effects on firm performance among the Kenyan stockbrokerage firms. This was important to also test the inter-relationship between firm performance and CG mechanisms.

### **3.3 Target Population**

The target population for the study were all the licensed stockbrokerage firms listed with CMA as at end of 2012 (Appendix IV). According to the CMA (2012) there are 19 listed firms. Most of the firms have their headquarters in Nairobi County and this was convenient in terms of time and accessibility to the researcher as recommended by Cooper & Schindler (2008) since the

researcher is in the stockbrokerage sector and thus access to key informants and respondents was possible.

### **3.4 Sample and Sampling Method**

The Capital Markets Authority is an independent public agency in Kenya established by an Act of Parliament, Cap 485 A, under the Ministry of Finance in 1990. The CMA is a regulating body charged with the prime responsibility of supervising, licensing and monitoring the activities of market intermediaries, including the stock exchange and the central depository and settlement system and all the other persons licensed under the Capital Markets Act.

Just like any other industry, the capital markets industry operates within a certain regulatory framework which the players in this industry must adhere to in the course of offering their services. Since inception, the Authority has strived to deepen and broaden the capital markets by developing a regulatory framework that facilitates the development of new financial products and institutions through research and ensuring fairness and orderliness in the capital markets industry. It was from the CMA licensees that the sampling frame was drawn.

In order to select the firms, the most robust sampling was used. The best sampling is probability sampling, because it increases the likelihood of obtaining samples that are representative of the population. Probability samples are selected in such a way as to be representative of the population. They provide the most valid or credible results because they reflect the characteristics of the population from which they are selected. Each individual in the population of interest has an equal likelihood of selection. The key to random selection is that there is no bias involved in the selection of the sample. Any variation between the sample characteristics and the population characteristics is only a matter of chance (Orodho & Kombo, 2002).

Based on Orodho & Kombo, (2002) who outlined that sampling is the procedure used to gather things, places or people to study, the study sampled the entire population of nineteen (19) stockbrokerage firms and had 17 respondents form the sample size as presented next in Table 3.1 next.

Table 3.1: Sample Size

<b>Company</b>	<b>Target respondent</b>	<b>Number of Respondents</b>
Afrika Investment Bank Ltd	Board Chair, CEO	2
ABC Capital Ltd	Board Chair, CEO	2
African Alliance (Kenya) Securities Ltd	Board Chair, CEO	2
Apex Africa Capital Ltd	Board Chair, CEO	2
CFC Stanbic	CEO	1
Discount Securities Ltd	Board Chair	1
Drummond Investment Bank Limited	Board Chair, CEO	2
Dyer & Blair Investment Bank Ltd	Board Chair, CEO	2
Faida Investment Bank Ltd	Board Chair, CEO	2
Genghis Capital Ltd	CEO	1
		17

### **3.5 Data Collection**

The study used a questionnaire as the main instrument to collect data from the respondents. Questionnaires are the most appropriate given the research objectives (Mellenbergh, 2008), respondents are given time to fill-in the questionnaires, do not require as much effort as for the verbal and telephone interviews and are easier to classify the data given in the closed ended questions making it easier to compile data.

The questionnaires were administered face-to-face to the respondents to enable the respondents to ask for clarification. Some respondents were located out of the CBD and to reach them, they were first telephoned and then sent the questionnaire via email. Later, additional telephone calls were done to ensure quick response. For those within reach, personal visits were made in order to collect the data faster and get a prompt response.

### **3.6 Pilot Test**

Since the purpose of pilot testing was to determine the accuracy of the data collection instrument, a pretest was first conducted using a similar target group of 8 people. Adjustments were then made to the instrument to get the final questionnaire.

### **3.7 Validity**

Rousson, Gasser & Seifer (2002) cited validity as the degree by which the sample of the test items represents the content the test is designed to measure. To establish the validity of the study, Construct Validity test was used; Face validity and internal construct validity. The face validity test was undertaken by administering the questionnaire as a pilot test prior to field work. The feedback gotten was then used to improve the instrument.

To establish the internal construct validity of the study, the construct validity test was used as reported under the data analysis section. Internal construct validity is concerned with the extent to which a particular measure relates to other measures in a way that is consistent with theoretically derived hypotheses concerning the concept. Construct validity defines how well a test or experiment measures up to its claims (Mugenda, 2008).

### 3.8 Reliability

According to Trochim & William (2006) reliability has to do with the quality of measurement. Reliability refers to the consistency of measurement and is assessed using the internal consistency reliability test. This test is preferred due to the fact that it does not require either splitting of a scale or the subject retaking the test for a given construct. It requires a single administration and provides a unique quantitative estimate of the internal consistency of a scale. Since Cronbach's Alpha is the most commonly used measure of co-efficient of internal consistency, the study adopted the Cronbach's Alpha. Reliability of the study was to investigate the relationship between: the board, the audit committee and the code of conduct which was measured using the Cronbach's Alpha;

$$\text{Alpha} = \frac{Nr}{(1 + r(N - 1))}$$

r is the mean inter-item correlation

N is the number of items in the scale

A co-efficient of 0.70 or more implies that there is a high reliability of data (Saunders, Lewis & Thornhill, 2009). The study therefore used 0.70 as a bench mark to determine the reliability of the questionnaire to be used. The questionnaire in Appendix III was subjected to Cronbach's alpha test and the 44 item instrument resulted  $\alpha = 0.854$ , meaning the questionnaire was very reliable.

### 3.9 Data Analysis

Since the study used the Likert-Scale, they minimized subjectivity and made it possible to carry out quantitative analysis (Nordin, 2009). The data collected was first cleaned, coded and systematically organized in a manner that would facilitate analysis using the SPSS, which offers extensive data handling capabilities and numerous statistical analysis routines that can analyze small and large data. From the data collected, descriptive statistics were conducted using tables to show the mean and standard deviation.

The quantitative data was analyzed using descriptive statistics. In specific, the study used the mean which is the average of the sample size and standard deviation which is a distribution, or

pattern, formed by many individual data values. Graphical and numerical methods of central tendency and measures of variability were also used to make an analysis of the quantitative data that was collected.

Saunders et. al (2009) insisted on the importance of descriptive analysis since it forms the basis of correlation and experimental studies emerge. It provides issues that should be focused on leading to the identification of areas of recommendation of future studies. Linear regression was carried out to measure the relationship between variables and also establish the strength of linear association between the variables. The study used non-parametric statistics Spearman rank correlation co-efficient test as the statistics test which assesses the linear correlation between two variables (Patrick, Smith& Pharm, 2009).

### 3.9.1 Linear Model specification

$$P = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \epsilon$$

P = Firm Performance (turnover)

X<sub>1</sub> = the Role of the Board

X<sub>2</sub> = Audit Committee

X<sub>3</sub> = Code of Conduct

$\beta_0, \beta_1, \beta_2$  and  $\beta_3$  are beta coefficients

### 3.10 Summary

Chapter three prescribed the approach to the data collection and the methodology. It also presented the target population, the sample and the procedure for the data analysis. Defining and designing a proper approach for data collection and analysis was important, as the results, conclusions and recommendations were dependent on this.

## CHAPTER FOUR: PRESENTATION OF RESEARCH FINDINGS

### 4.1 Introduction

Having presented the research rationale earlier, chapter four now presented the research findings. It presented the response rate, the demographic profile, and the profiled data on corporate governance mechanisms covering the board, the audit committee and the code of conduct, and the inferential statistics. Linear regression was used to investigate the corporate governance mechanisms and determine their effects on firm performance among the Kenyan stockbrokerage firms and relate the variables to provide more in-depth insights for the correct conclusion. The findings were presented in descriptive tables using the mean, standard deviation and kurtosis.

### 4.2 Response Rate

More questionnaires than target were distributed to cater for response rate and hence twenty questionnaires were distributed and seventeen were received with responses, an equivalent of 85% response rate. According to Saunders et. al (2009), a 50% response rate is adequate, 60% good and above 70% rated very good, the response rate in this case of 85% was very good, as presented next

#### Response Rate

Questionnaires distributed	Questionnaires received	Response rate
20	17	85%

### 4.3 Demographic Profile

The rationale of the study was to investigate the corporate governance mechanisms and determine their effects on firm performance and it was important to first collect and aggregate the stockbrokerage firms' annual turnovers over a four year period (2009 – 2012). From the findings, there was a decrease in turnover from the year 2010, as presented in figure 4.1 next and the individual stockbrokerage firm performance is presented in table 4.2 next.

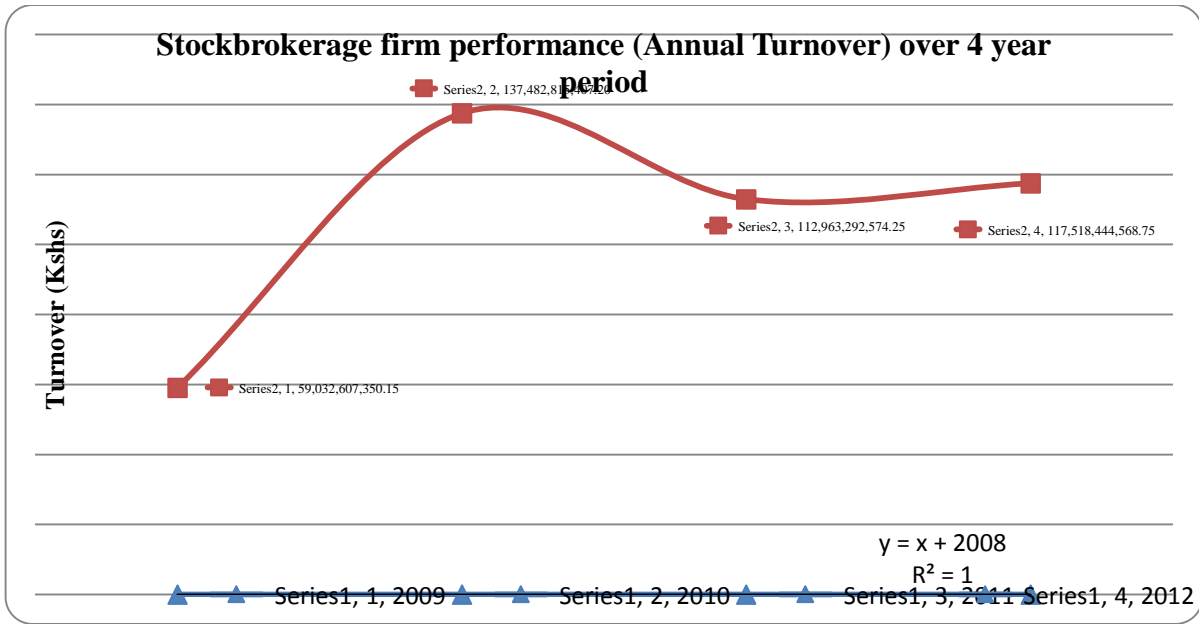


Figure 4.1: Aggregate Firm Performance (Annual Turnover) of Stockbrokerage firms

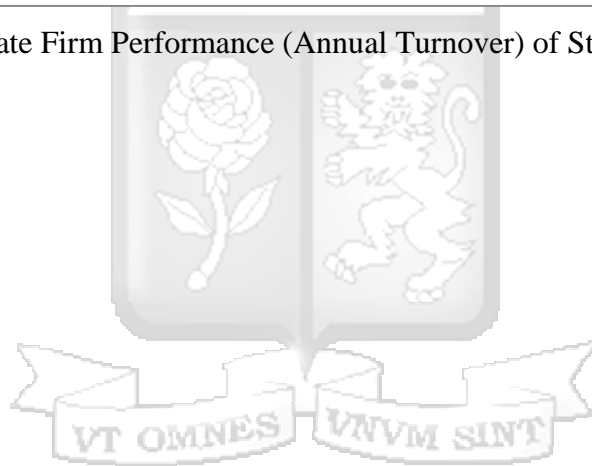


Table 4.2: Firm Performance (Annual Turnover) of Stockbrokerage firms (2009-2012)

ANNUAL TURNOVER					
Year / Stockbrokerage Firm	2009	2010	2011	2012	Analysis
Firm 1	231,642,219.40	515,290,687.05	480,327,179.10	358,464,230.55	Decrease in turnover even after the CMA 2011 guidelines
Firm 2	10,230,205,656.10	20,802,307,996.90	11,899,316,518.80	21,168,303,500.60	Decrease then increase of turnover in 2012
Firm 3	1,269,961,283.30	3,109,790,144.20	1,599,765,688.30	1,333,744,959.90	Decrease in turnover even after the CMA 2011 guidelines
Firm 4	171,323,515.05	279,965,750.85	2,390,818,411.40	4,261,702,628.20	Turnover increase
Firm 5	5,123,866,875.85	16,923,468,083.65	16,822,295,570.60	17,726,351,802.80	Decrease then increase of turnover in 2012
Firm 6	742,807,377.70	4,934,941,192.55	4,898,482,483.95	4,424,347,368.45	Decrease in turnover even after the CMA 2011 guidelines
Firm 7	4,269,840,881.05	6,956,355,906.10	3,397,264,855.55	3,047,306,074.65	Decrease in turnover even after the CMA 2011 guidelines
Firm 8	507,437,126.20	1,443,113,992.70	739,825,208.40	661,603,897.30	Decrease in turnover even after the CMA 2011 guidelines
Firm 9	2,790,652,452.65	12,792,969,158.05	8,572,507,510.50	6,790,682,494.25	Decrease in turnover even after the CMA 2011 guidelines
Firm 10	6,770,378,442.05	15,494,811,457.15	8,414,794,969.80	7,714,753,236.30	Decrease in turnover even after the CMA 2011 guidelines
Firm 11	2,020,280,294.55	3,883,207,638.35	6,016,656,037.00	3,780,294,007.40	Decrease in turnover even after the CMA 2011 guidelines
Firm 12	14,096,239,311.80	33,801,584,768.00	33,013,935,444.85	25,304,635,018.00	Decrease in turnover even after the CMA 2011 guidelines
Firm 13	10,406,800,632.80	16,267,754,007.65	14,291,117,152.25	20,618,480,818.05	Turnover decrease in 2011 only
Firm 14	302,213,387.60	233,778,399.00	72,032,362.00	209,745,155.00	Decrease in turnover even after the CMA 2011 guidelines
Firm 15	12,706,210.00	0.00	305,218,816.75	84,600,177.20	Decrease in turnover even after the CMA 2011 guidelines
Firm 16	433,765.00	1,262,650.00	33,839,220.00	7,386,800.10	Decrease in turnover even after the CMA 2011 guidelines
Firm 17	82,690,034.05	24,072,700.00	11,869,845.00	26,042,400.00	Turnover decrease in 2011 only
Firm 18	824,385.00	14,721,125.00	2,707,800.00	0.00	Decrease in turnover even after the CMA 2011 guidelines
Firm 19	2,303,500.00	3,419,750.00	517,500.00	0.00	Decrease in turnover even after the CMA 2011 guidelines
<b>Total</b>	<b>59,032,607,350.15</b>	<b>137,482,815,407.20</b>	<b>112,963,292,574.25</b>	<b>117,518,444,568.75</b>	Decrease in turnover even after the CMA 2011 guidelines

The study collected the respondents' demographic profile, and from the findings, majority, 94% were educated to university level while the other 6% were educated to middle level college, as presented in figure 4.2 next. This concurred with the findings that stockbrokerage firms employ qualified personnel who enhanced production of high quality outcomes and effective quality improvement in financial investment (Brown & Duguid, 2003).

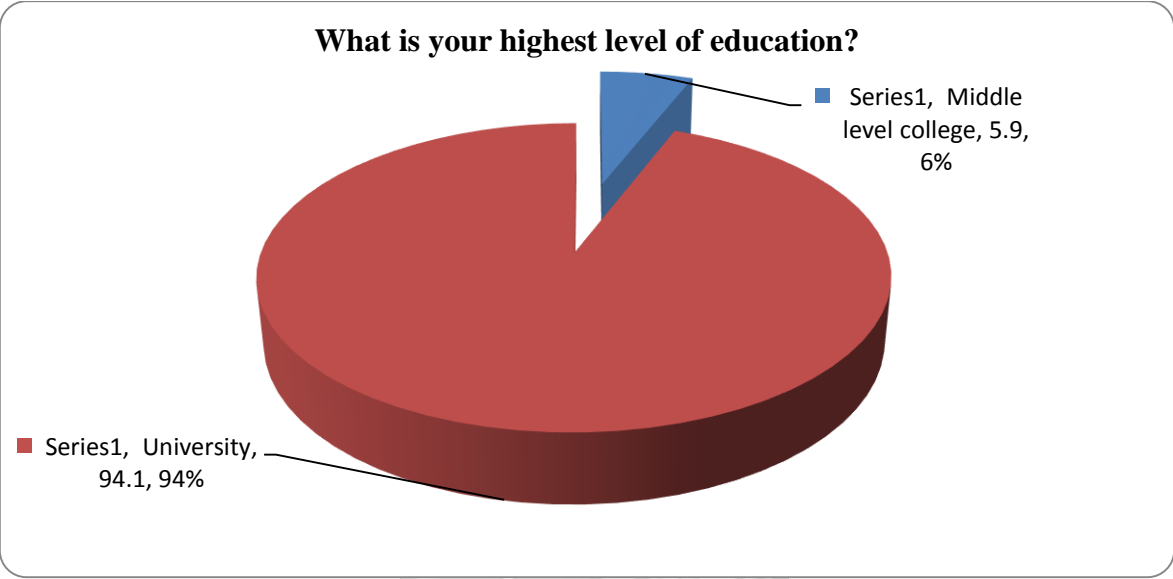


Figure 4.2: Level of education

The study collected the demographic profile of the stockbrokerage firms, since following the unprecedented growth of the Kenyan financial markets in the recent past, some stockbrokerage firms experienced significant financial difficulties forcing the Capital Markets Authority (CMA) to place them under receivership/statutory management. The study sought to determine the length of time the firm has been in existence, the ownership structure and if the stockbrokerage firm operates outside Kenya.

From the findings, most (35.3%) had operated for over 16 years in Kenya, 17.6% had operated for between 11 to 15 years and an equal number for between 0 to 10 years, as presented in figure 4.3 next.

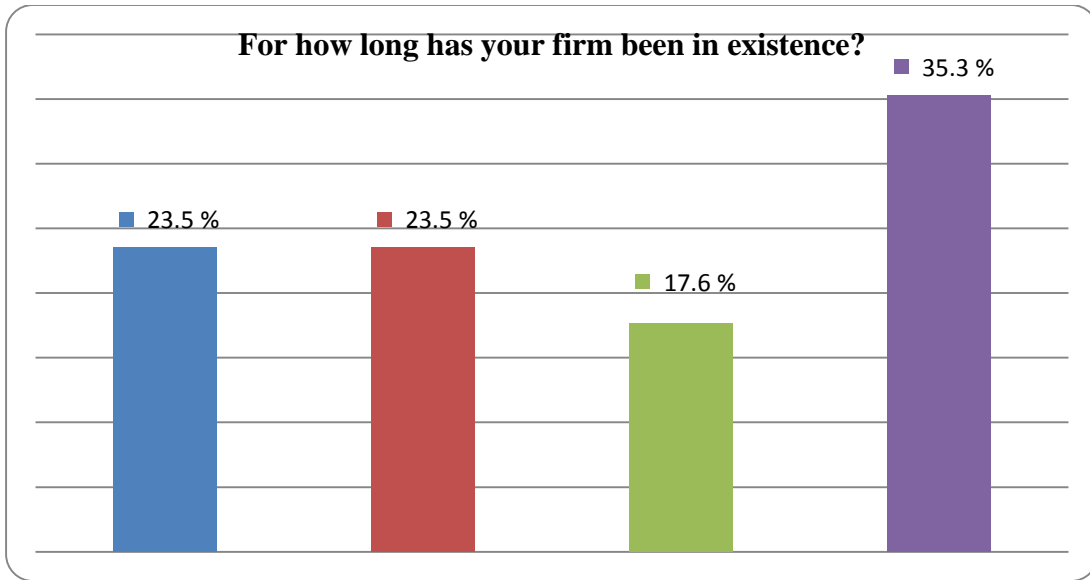


Figure 4.3: Length of operation

With regards to the ownership of the stockbrokerage firms, 59% were locally owned and 23% had a foreign/local ownership, as presented in figure 4.4 next. Stockbrokerage firms are licensees of the Capital Markets Authority (CMA) and the findings conform to CMA (2012).

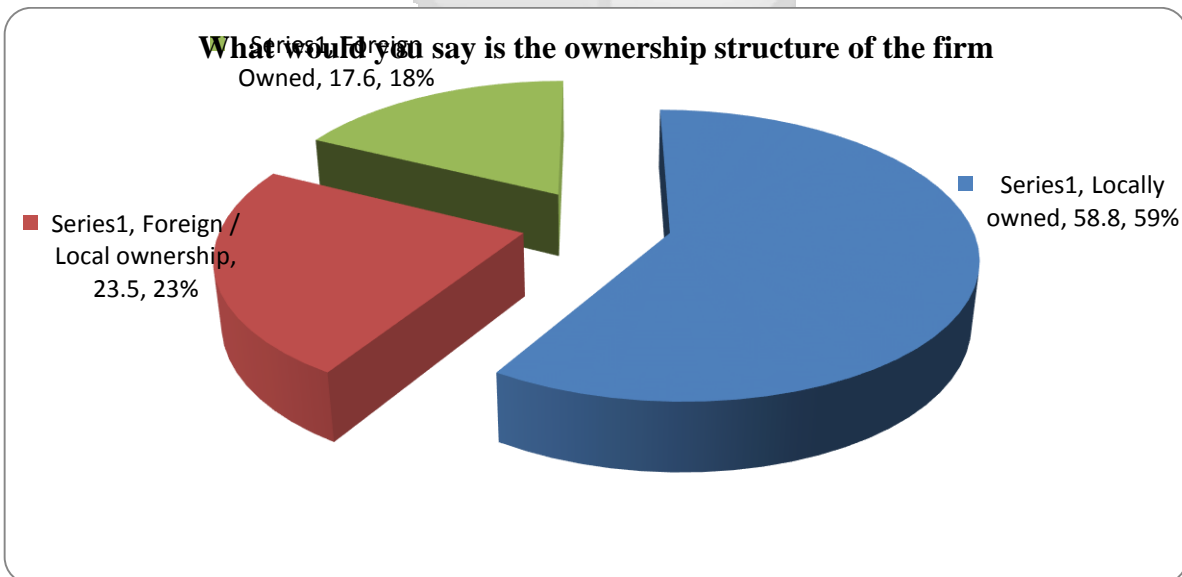


Figure 4.4: Ownership

Of the 35% stockbrokerage firms that stated they operate outside of Kenya, as presented in figure 4.5 below, the respondents stated that they operate in Southern Africa and Europe. The operations are also different and the findings concur with Giuseppina (2011) who noted that the degree of investor protection is determined by the country's system.

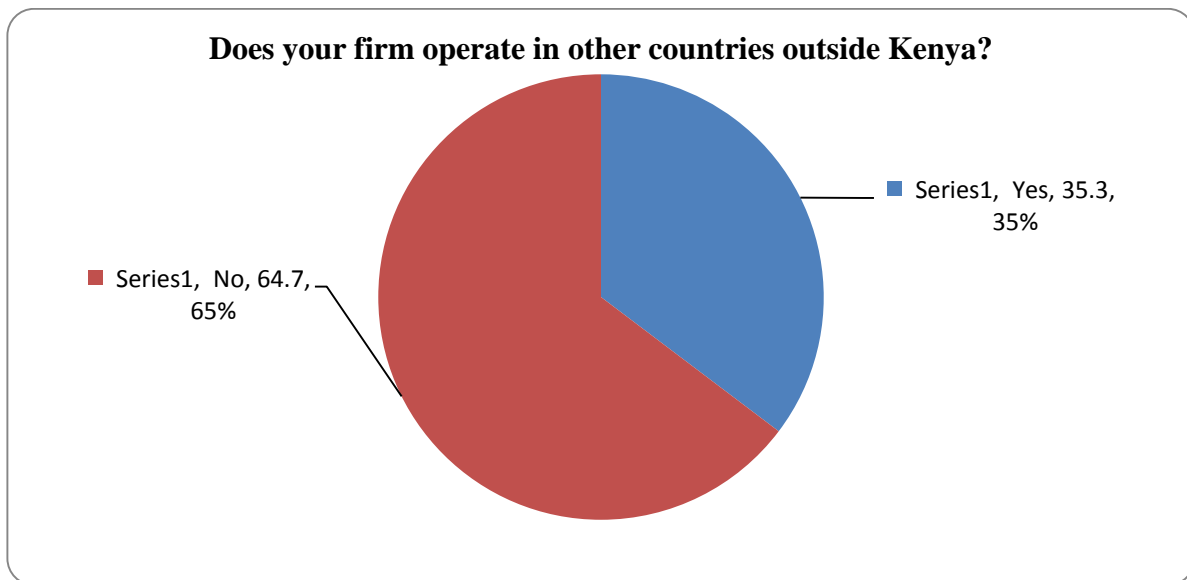


Figure 4.5: Operation outside Kenya

#### 4.4 Extent of Implementation of CMA Regulation on Corporate Governance

The first specific objective of the study was to assess the extent of implementation of CMA regulation on Corporate Governance in stockbrokerage firms. The study looked at the implementation of CMA regulation in terms of; the board, audit committee and code of conduct. The findings are presented next.

##### 4.4.1 The Board

From the findings, more than half of the stockbrokerage firms, 58.8% had 8 board members. Only 23.5% had 4 board members, as presented next in figure 4.6. What about 17.6%??

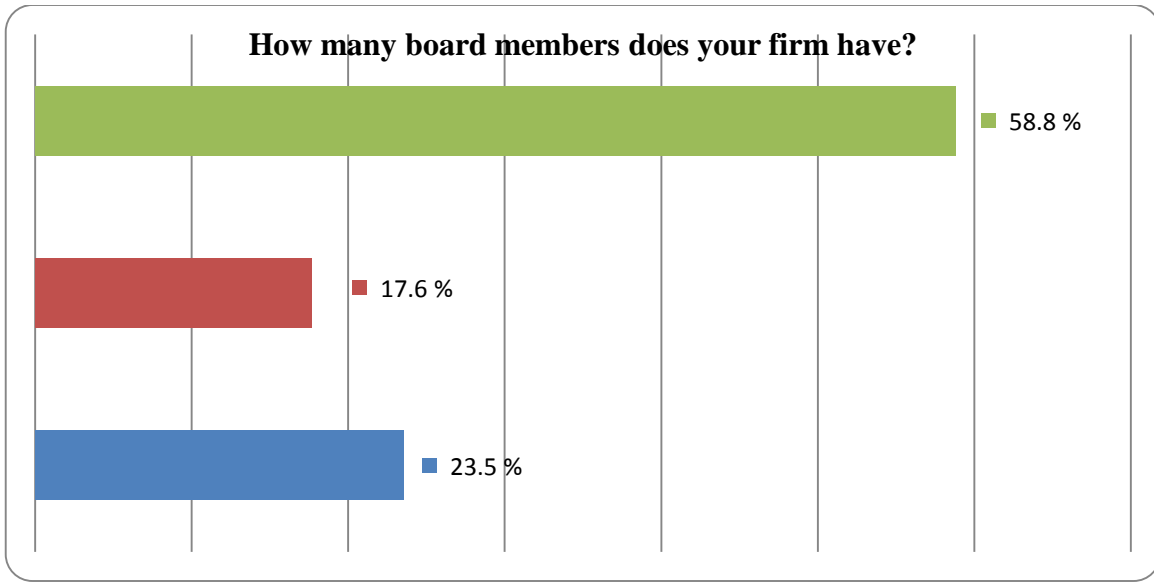


Figure 4.6: Number of board members

All the respondents (100%) stated that the board members do not have a fixed term, a finding similar to Statoil (2011) who also noted that the legal and governance duties of the board vary according to the company law and corporate governance codes of the jurisdiction in which it operates. Regardless of any jurisdictional differences, a primary intent of most codes is to ensure that boards achieve a balance between governance, oversight and risk management on the one hand and strategic challenge and management support on the other.

53% of the respondents affirmed that their board members, chairman of the board and the CEO are appointed through a recruitment process / shareholder recruitment process, as presented in figure 4.7 next. 35% stated that their board members, chairman of the board and the CEO are appointed by the owners. All the respondents, 100% cited it would not make a difference if the process of their board members, chairman of the board and the CEO were different.

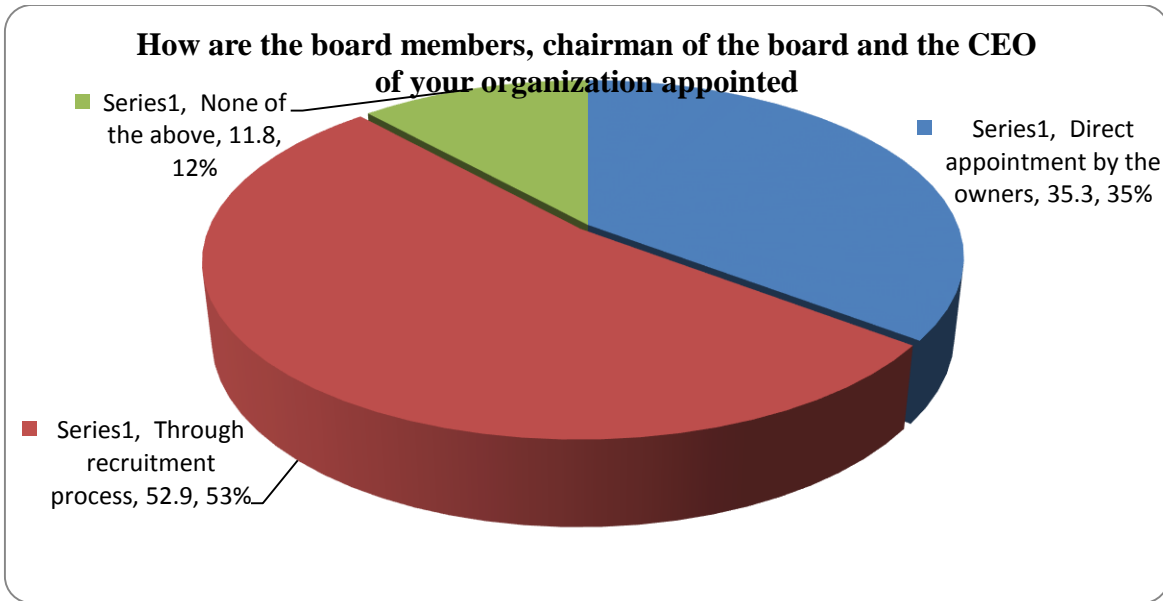


Figure 4.7: Appointment of board members

More than three quarters, (82%) of the respondents, stated that the membership of their firm board members is diversified in terms of their background and skills, as presented in figure 4.8 next. The respondents stated that following the diversity of the board members, there is international representation; board members are vetted with criterion, are well known and have broad knowledge and experience.

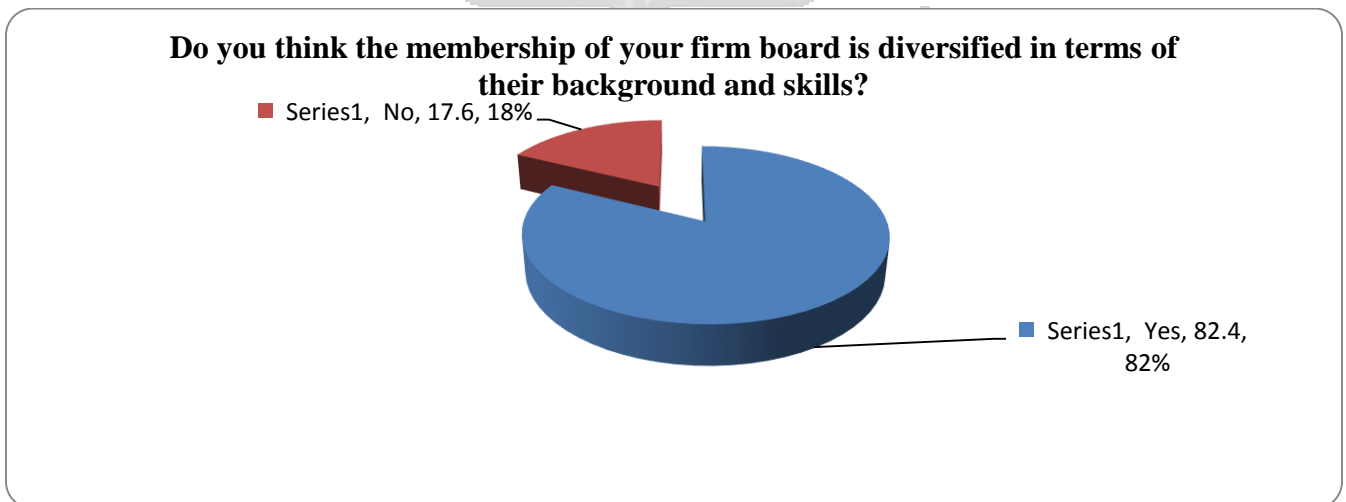


Figure 4.8: Diversity of board membership

A major aspect of evaluating the corporate governance mechanisms and their implication on firm performance is the board. The responses in this section were based on a five Likert scale of: 1=strongly disagree, 2= disagree, 3= Neutral, 4= agree, and 5= strongly agree. The respondents were requested to indicate their level of agreement regarding if the board members educational qualification is sufficient to carry out their duties in the firm, if their professional qualification is considered before appointment, if their actions are independent from outside influence, if the independent director's proportion to the executive director's is as per the CMA guidelines, whether the board members are honest and objectively accountable in their dealings, whether the board ensures that the firm conforms to legislation and government policies as well as achieve agreed outcomes, if the frequency of the board meetings is adequate to determine policy decisions and if there exists an adequate succession plan for the board members in the firm. From the findings, most agreed as shown by (mean  $\geq$  4), as presented in table 4.3 next.

Table 4.3: Summary of mean and standard deviation - the Board

	Mean	Std. Deviation
The board members educational qualification is sufficient to carry out their duties in the firm	4.41	0.618
The board members professional qualification is considered before appointment	4.35	0.606
The board members action is independent from outside influence	4.12	1.166
The independent directors proportion to the executive directors is as per the CMA guidelines	4.59	0.507
The board members are honest and objectively accountable in their dealings	4.35	0.493
The board ensures that the firm conforms to legislation and government policies as well as achieve agreed outcomes	4.35	0.606
The frequency of the board meetings is adequate to determine policy decisions	4.47	0.624
There exist adequate succession plan for the board members in the firm	4.00	1.000
Overall	4.33	0.688

#### 4.4.2 Audit Committee

From the findings of the study, all (100%) of the stockbrokerage firms have an audit committee. The finding can be attributed to the CMA guidelines and regulations. Following the need to strengthen the corporate governance and safeguard public interests in the capital markets industry the Government undertook a comprehensive reform program to put in place a robust supervisory and regulatory framework in the capital markets (Government of Kenya, 2012).

The study sought to determine whether the audit committee is responsible for recommending an external auditor, ensuring the soundness and quality of internal accounting and control practices of the firm, concerned with monitoring the external auditor's independence from senior management, conduct frequent meetings and if the firm has a well developed governance manual.

The findings from the responses were based on a five Likert scale of: 1=not at all, 2= Little Extent, 3= Moderate Extent, 4= Great Extent and 5= Very great extent. From the findings, as presented in table 4.4 next, the mean is greater than 4 and hence the respondents strongly agreed that the audit committee is responsible for recommending external auditor, the soundness and quality of internal accounting and control practices, is concerned with monitoring, has meetings frequently and has a well developed manual.

Table 4.4: Summary of mean and standard deviation - audit committee

	Mean	Std. Deviation
The audit committee is responsible for recommending external auditor	4.24	0.970
Responsible for ensuring the soundness and quality of internal accounting and control practices of the firm	4.47	0.624
Concerned with monitoring the external auditor's independence from senior management	4.18	0.951
The frequency of meetings by the audit committee is considered to be adequate	4.41	0.507
The organization has a well developed governance manual	4.12	0.781
Overall	4.28	0.645

Since the CMA Act was amended to introduce greater professionalism and greater accountability with respect to executive management and senior managers owning more than 25% of shares (CMA, 2012), the study sought to determine the importance to which the stockbrokerage firms place on the audit committee, the directors nomination committee, the directors compensation committee and the availability of code of conduct.

From the findings, the mean is greater than 4 implying that the respondents have placed importance on the audit committee, the directors’ nomination committee, the director’s compensation committee and the availability of code of conduct. However, from the findings, the director’s nomination committee’s importance is rated from least important to most important as presented in table 4.5 below.

Table 4.5: Importance to factors affecting CG practices

	Mean	Std. Deviation
Audit Committee	4.38	0.500
Directors Nomination committee	4.13	0.957
Directors Compensation Committee	4.31	0.704
Availability of code of conduct	4.56	0.512
Overall	4.35	0.614

To determine the extent of conformance and compliance, the respondents’ responses were based on a five Likert scale of: 1=strongly disagree, 2= disagree, 3= Neutral, 4= agree, and 5= strongly agree. The respondents were requested to indicate their level of agreement regarding upholding the firms’ values and ethics, guidance on policies, procedures, processes, principles and tasks, confidentiality, security and fraud controls, compliance with legislative guidelines as required and quality assurance.

As presented in table 4.6 next, the mean was between 3.0 and 3.9 hence the respondents are neutral. They neither agree nor disagree.

Table 4.6: Elements of conformance and compliance - audit committee

	Mean	Std. Deviation
Upholding the firms' values and ethics	3.88	1.269
Guidance on policies, procedures, processes, principles and tasks	3.71	1.160
Ensuring and maintaining confidentiality	3.56	1.413
Enforcing security and fraud controls	3.71	1.312
Compliance with legislative guidelines as required	3.59	1.417
Quality assurance	3.71	1.263
Overall	3.69	1.113

#### 4.4.3 Code of Conduct

From the research findings, all (100%) of the stockbrokerage firms have a code of conduct. The study sought to determine if the Code of Conduct is upheld by the Board and all staff, is inculcated in job descriptions, meetings with the agenda on code of conduct are held and whether the organization has a well developed code of conduct manual. From the findings, the code of conduct manual is rated lowest. All attributes have the mean greater than 4, which implied that the respondents agreed. This is presented in table 4.7 next.

Table 4.7: Summary of mean and standard deviation - code of conduct

	Mean	Std. Deviation
The Code of Conduct is upheld by the Board and all staff	4.59	0.507
Code of conduct is inculcated in job descriptions	4.35	0.493
There are meetings with agenda on code of conduct	4.06	0.748
The organization has a well developed code of conduct manual	4.18	0.951
Overall	4.29	0.562

The study collected data on how the CMA rules introduced in 2011, have been implemented in the stockbrokerage firm. From the findings 35% do not know how they have been implemented (35%).

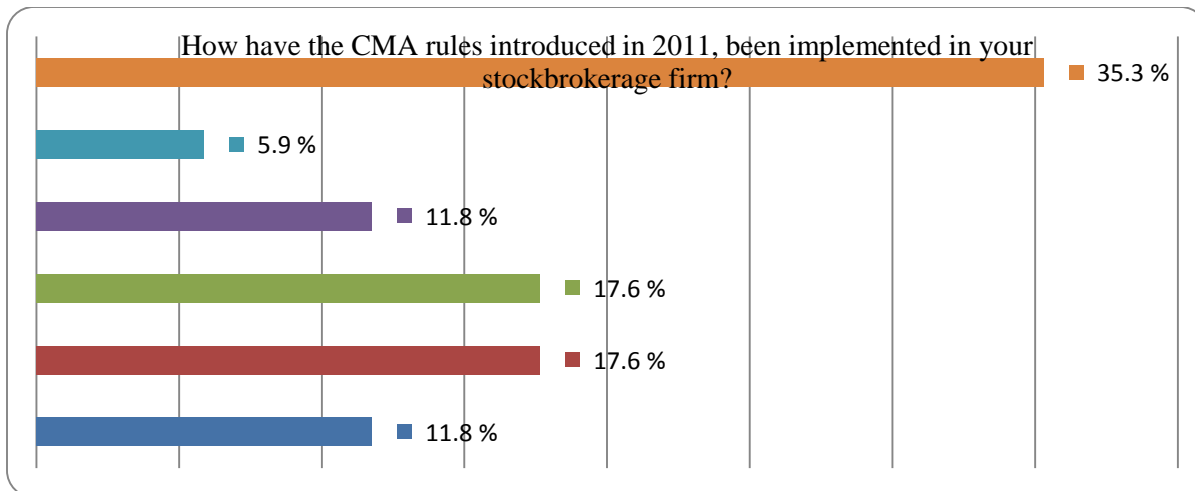


Figure 4.8: How CMA rules have been implemented

#### 4.5 Challenges in implementing CG mechanisms

The second objective of the study was to identify the challenges in implementing the corporate governance mechanisms. From the findings of the study, the challenges in implementing the CMA rules were identified as; understanding the specific rules, convincing clients to abide by the new changes, the redundancy of the rules despite the stiff competition, coordinating the same among the branch network and team work among staff, as presented in figure 4.9 next. Majority don't know the challenges, which can be attributed to the fact that the CG policies only targeted CEOs.

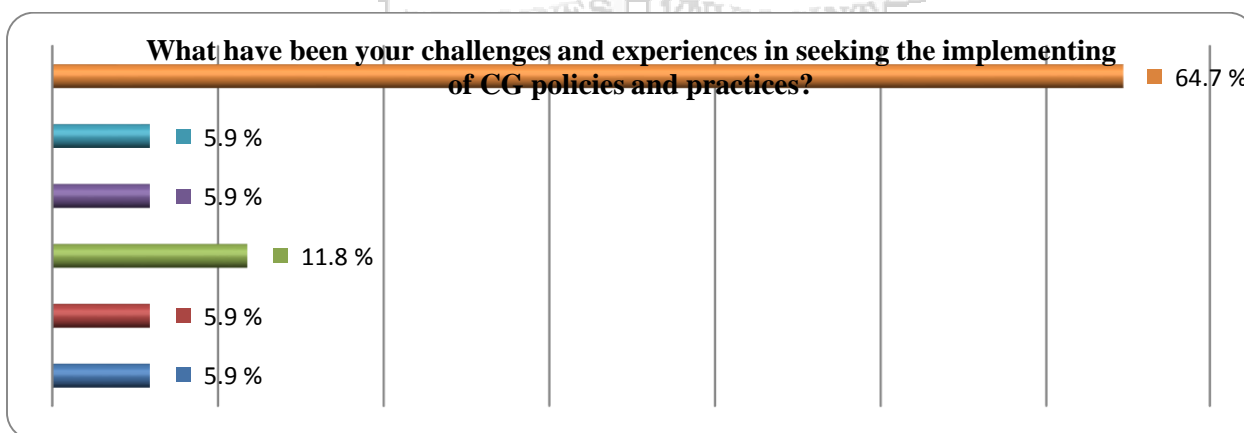


Figure 4.9: Challenges in implementing CMA rules

#### 4.6 Relationship between CG mechanisms and Firm Performance

The study proposed that there exists a relationship between corporate governance mechanisms and firm performance. Correlation analysis was used to establish the strength of the relationship while regression analysis was used to come up with the model for forecasting purposes. Further hypothesis test was done to check on the statistical significance of the model parameters.

Table 4.8: Coefficient Correlations

Model		Code of conduct	Audit committee	Board
1	Correlations	Code of conduct	1.000	
		Audit committee	.060	1.000
		Board	-.325	-.138

Dependent Variable: Turnover

Predictor variables are said to be related to each other (multicollinearity) if the correlation coefficient between them is greater than 0.5. In such a situation one of them must be removed from the model. As shown in table 4.8 above, there is no problem of multicollinearity (coefficients <0.5), thus all the three predictor variables could be used in forecasting turnover amongst stock brokerage firms

Table 4.9: Model Summary

Model		R	Adjusted R	Std. Error of the Estimate	Change Statistics					
					R Square	F Change	df1	df2	Sig. F Change	
dimension0	1	.698 <sup>a</sup>	.487	.332	4462.76863	.487	3.159	3	10	.043

a. Predictors: (Constant), code of conduct, audit committee, board

The "**R Square**"(coefficient of determination) a value of 0.487, indicates a moderate level of prediction. It further indicates that 48.7% of the variations in firm performance (turnover) can be

explained by the changes in code of conduct, audit committee, board, leaving 51.3% unexplained (error term).

Table 4.10: ANOVAb

Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	1.887E8	3	6.291E7	3.159	.043 <sup>a</sup>
	Residual	1.992E8	10	1.992E7		
	Total	3.879E8	13			

a. Predictors: (Constant), code of conduct, audit committee, board

b. Dependent Variable: turnover

The *F*-ratio in the **ANOVA** table tests whether the overall regression model is a good fit for the data. The table shows that the independent variables statistically significantly predict the dependent variable,  $F(3, 10) = 3.159, p = .043 < .05$  (i.e., the regression model is a good fit of the data).

Table 4.11: Coefficients

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	17754.764	18676.254		.951	.364
	Board	6287.067	2833.814	.537	2.219	.041
	Audit committee	5894.869	2469.294	.547	2.387	.038
	Code of conduct	3699.695	3277.136	.273	1.129	.285

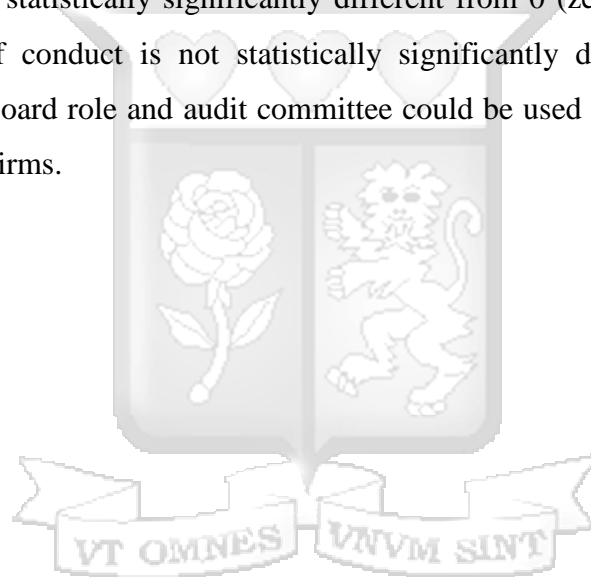
a. Dependent Variable: turnover

The general form of the equation to predict performance of the firms (turnover) from code of conduct, audit committee, board, is:

$$\text{Predicted Firm Performance (turnover)} = 17754.764 + (6287.067 * \text{board}) + (5894.869 * \text{Audit committee}) + (3699.695 * \text{Code of conduct})$$

This is obtained from the Coefficients table (Unstandardized coefficients), as shown above: Unstandardized coefficients indicate how much the dependent variable varies with an independent variable, when all other independent variables are held constant, that is, for every one unit increases in the role of board, firm performance increases by 6287.067 other factors held constant.

Statistical significance of the independent variables tests was used to test whether the Unstandardized coefficients are equal to 0 (zero) in the population. If  $p < .05$ , then one can conclude that, the coefficients are statistically significantly different to 0 (zero). The corresponding  $p$ -value are located in the "Sig." columns, respectively, indicates that board role and audit committee are statistically significantly different from 0 (zero) i.e.  $p\text{-value} < 0.05$ . On the other hand Code of conduct is not statistically significantly different from 0 since  $p\text{-value} = .285 > 0.05$ . Thus board role and audit committee could be used to predict performance of Kenyan stockbrokerage firms.



## CHAPTER FIVE: DISCUSSION

### 5.1 Introduction

This chapter serves to demonstrate the achievements of the objectives set out at the initiation of the study and presents in brief the results of these efforts in line with other studies done on the same topic. Discussion of the findings was based on the study objectives as follows.

### 5.2 The extent of implementation of CMA regulation on Corporate Governance in stockbrokers firms

From the findings of the study, all the stockbrokerage firms had a board of between 4 to 8 members; this is supported by the research done by Bassen & Zollner (2007) in the literature review, which found out that Board composition, played an important role in facilitating effective mechanisms of running internal affairs of stockbrokerage firms.

In order to comply with CMA's Market Intermediaries Regulations 2011 Framework, that is, the stockbrokerage firms must establish a corporate governance framework and the board shall review its corporate governance structure annually and the results of such review should be documented; the study found out that board members had sufficient educational qualification to carry out their duties in the firm, the independent directors' proportion to the executive directors complied with the CMA guidelines and the frequency of the board meetings were adequate in determining policy decisions. The findings concur with those of Fama & Jensen, (1983), that is, with a robust board structure in a stockbrokerage firm, the risk of collusion with top management is reduced, as independent directors are expected to ensure that the law is respected and to limit agency problems. Also Rosenstein & Wyatt (1990) observe a positive market reaction to the appointment of independent directors. Perry and Shivdasani (2005) explain that firms with a majority of outside directors are more likely to restructure following performance declines, and more determined in doing so.

Internal audit is an independent management function, which involves a continuous and critical appraisal of the functioning of an entity with a view to suggest improvements thereto and add value to and strengthen the overall governance mechanism of the entity, including the entity's strategic risk management and internal control system. The audit committee is an integral element of accountability and governance. It plays a key role with respect to the integrity of the entity's financial information, its system of internal controls, and the legal and ethical conduct of management and employees. Audit committee responsibilities include approving the overall audit scope, recommending the appointment of the external auditor, overseeing the entity's financial statement and internal controls, helping to ensure that the audit is conducted in a cost-effective manner, and risk management oversight. An audit committee must have three important qualities in order to fulfill its duties: independence, communication, and accountability, (George, 2005). The study findings also indicated that all the stockbrokerage firms had an audit committee which is responsible for recommending an external auditor, ensuring the soundness and quality of internal accounting and control practices of the firm, concerned with monitoring the external auditor's independence from senior management, conducts frequent meetings and has a well developed governance manual.

Code of Conduct sets the basic rules people must follow and explains how values should guide all of decisions. It highlights the Principles, values, standards, or rules of behavior that guide the decisions, procedures and systems of an organization in a way that contributes to the welfare of its key stakeholders, and respects the rights of all constituents affected by its operations. The respondents were in agreement that; the code of conduct is upheld by the board and all staff, code of conduct is inculcated in job descriptions, meetings with agenda on code of conduct are held frequently and the organizations have a well developed code of conduct manual. The findings concur with those of Lang & Jagtiani (2010) who acknowledged that operational managers need to act in the interests of the owners of the entities and other stakeholders and sound corporate governance encourages the efficient use of resources and provides for accountability for the stewardship of those resources by managers.

### **5.3 The challenges in implementing corporate governance mechanisms and practices among the Kenyan stockbrokerage firms**

Corporate governance practices differ among firms and organizational forms and include the determination of ownership structure, accounting rules, protection of minority shareholders and board of director's powers. In particular, it aims at regulating the separation between ownership and control and at balancing limits on managerial discretion and minority shareholders' protection. One factor receiving increased attention in international business is a country's corporate governance system and practices and the study collected data on the challenges facing the implementation of the corporate governance policies.

From the findings, the key challenges were; understanding the specific CMA 2011 rules among all staff, convincing clients to abide by the new changes, the redundancy of the rules despite the stiff completion, coordinating the corporate governance policies among the branch network promoting team work among staff and conflicts between the managers and shareholders (agency problem). The challenges concur with the ones identified in the study done by Agrawal & Knoeber (1996), that is, agency problems arise within a firm whenever managers have incentives to pursue their own interests at shareholder expense as well as Bassen & Zollner (2007) findings which acknowledged that the reason that led to the closure of stockbrokerage firms in developed countries, was the lack of proper governance structures that led to manipulations of balance sheets.

### **5.4 Relationship between Corporate Governance Mechanisms and Firm Performance among the Stockbrokerage Firms in Kenya**

The study used regression analysis to find the association between boards, audit committees, code of conduct and performance of Kenyan stockbrokerage firms. The finding indicated that the model was moderately significant ( $R^2=48.7\%$ ). It was noted that board, audit committee and code of conduct were positively related with the firm performance. The results have supported studies by Rosenstein & Wyatt (1990).

Though the study posits that firm performance (turnover) depend on board, audit committee and code of conduct (conceptual framework), it was found out that Boards and audit committees

were individually related to performance of Kenyan stockbrokerage firms (statistically significant) while code of conduct was not linearly related with performance of Kenyan stockbrokerage firms. It reaffirms what some of the previous researcher (Bauer et al. (2004) have found, that there is a positive relationship between corporate governance and firm performance



## CHAPTER SIX: CONCLUSION AND RECOMMENDATIONS

### 6.1 Conclusion

The general objective of the study was to determine the influence of corporate governance mechanisms on the firm performance measured in terms of annual turnover. The study findings revealed that Kenyan stockbrokerage firms have given prominence to corporate governance mechanisms issues and the rules introduced by the government and the regulator (CMA) were concerted efforts of all players in order to safeguard the integrity of the stock market, since promoting clear legal rules has emerged as a crucial new priority in the global liberalization process in order to give more guarantees to foreign investors and to encourage foreign and domestic investments.

The study established that not all hypothesized independent variables were statistically significant. Only board and audit committee influenced the stock brokerage firm performance, that is, the board and the audit committees are instrumental in managing the businesses in a professional manner. The reforms by the CMA were important in enhancing professional and operational capacity of the capital market institutions and intermediaries, setting up compliance and enforcement mechanisms, as well as enhancing the capital market infrastructure.

### 6.2 Recommendations

The study makes an important contribution in understanding Corporate Governance Mechanisms. It further brings out the factors that influence the relationship between Corporate Governance Mechanisms and Firm Performance among the Stockbrokerage Firms in Kenya. Arising from this study, the researcher makes the following recommendations.

To the policy makers; Impose regulations, specifically efficient corporate governance systems and rules are considered necessary to overcome the conflicts between manager (or controlling shareholders) and (non-controlling) shareholders, thus insuring that the latter's interests are protected. There is need of a mechanism to deal with the management and the supervisory

system as well as the legal and factual regulation framework for the interaction of management, board and stakeholders. In order to achieve this CMA, CDSC and NSE should review the guidelines and policies in conjunction with the board members of the stockbrokerage firms and other stakeholders.

It is recommended that future studies include other variables such as return on investments, net profit, shareholders value, quality of products/service, market share and customer satisfaction because they also measure firm performance. These findings will provide an increase in knowledge and a rich data base for future research, which can then be compared with the results of this study.

From the study, the respondents cited the need of client feedback system as a key recommendation because they felt that the customers do not understand the CG policies and therefore there is need to sensitize these people.

### **Areas of Further Research**

The Authority, CMA, led by the Board of Directors and supported by the Chief Executive together with the management, carries out its mandate of regulating and developing the Kenyan capital markets through a regulatory framework that is deliberately designed to meet this objective.

Just like any other industry, the capital markets industry operates within a certain regulatory framework which the players in this industry must adhere to in the course of offering their services. Since inception, the Authority has strived to deepen and broaden the capital markets by developing a regulatory framework that facilitates the development of new financial products and institutions through research and ensuring fairness and orderliness in the capital markets industry. The regulatory framework of the Authority is comprised of the following: Main Acts, that is The Capital Markets Act and The Central Depositories Act, 2000 and Other Regulations and Rules. There is need for other scholars to study the impact of these regulations on the sector.

## REFERENCES

- Adrian T. (2009). *Essentials for Board Directors: An A-Z Guide*, Bloomberg Press, New York.
- AfDB ( 2012). *African Economic Outlook*, Africa Development Bank, OECD, UNDP, UNECA
- Agrawal & Knoeber (1996). *Firm Performance and Mechanisms To Control Agency Problems Between Managers And Shareholders*. Wharton School, University of Pennsylvania
- Bassen, A. & Zöllner, C. (2007). *Corporate Governance und Unternehmenswert*, Wagenhofer, A. (Ed.), Controlling und Corporate Governance- Vol. 67 (1), pp 93-112
- Bauer, R., Guenster, N., & Otten R. (2004). Empirical Evidence on Corporate Governance in Europe. The Effect on Stock Returns, Firm Value and Performance, *Journal of Asset management* 5 (2) 91 – 104
- Bebchuk, L., Cohen, A., & Ferrell A, (2009). *What Matters in Corporate Governance?* Review of Financial Studies 22: 783 - 827.
- Beekes, W , Brown, P. & Chin, G. (2006). *Do better governed firms make more informative disclosures? Canadian evidence*, Lancaster University : The Department of Accounting and Finance, (Accounting and Finance Working Paper Series)
- Bhagat, S. & Black B. (2002). The non-correlation between board independence and long term firm performance, *Journal of Corporation Law* 27 Vol Issue page #
- Brown, L. & Caylor M., (2006). *Corporate Governance and Firm Operating Performance*. *Journal of Accounting and Public Policy* 25 (2006), pp. 409–434.
- Brown, J. S, Duguid, P. (2003). *“The Social Life of Information”*. Harvard Business Press City?

Carpenter, M & Westphal, J (2001). *The Strategic Context of External Network ties: Examining the Impact of director appointment on Board involvement in strategic decision making*. Academy of Management, 44(4), 639-660

CBK (2012). *Central Bank of Kenya*, Nairobi. Available at: [www.cbk.go.ke](http://www.cbk.go.ke) [accessed 11 February 2013]

CMA (2012). *Capital Markets Authority*, Nairobi. Available at: [www.cma.or.ke](http://www.cma.or.ke) [accessed 10 February 2013]

Cooper, D. , & Schindler, P. (2008). *Business Research Methods*, International Edition, 10th ed.

Crane. A & Matten. D. (2007) “*Business Ethics*” (2<sup>nd</sup> Ed). Oxford University Press.

Cremers, M., Nair, V (2005). *Governance Mechanisms and Equity Prices*. Journal of Finance 60, 2859–2894

Dine, J. (2000). *The Governance of Corporate Groups*. Cambridge Studies in Corporate Law 1

Donaldson, L. & Davis, J. (2004). *Board and Company Performance – Research Challenges the Wisdom*. Corporate Governance: An International Review, 2(3), 65-91

Dunlop, I., (2000). *The board of the future: Governance for a New Era*. Publisher & City

Dunne T & Helliar C, (2002). The Ludwig report: implications for corporate governance, *Corporate Governance*, Vol. 2 Iss: 3 pp. 26 – 31

Etzioni, A (2005). *Affective bonds and moral norms: A communitarian approach to the emerging global society*. Internationale Politik und Gesellschaft, 12(3): 127-143.

Fama, E., & Jensen M. (1983). *Separation of Ownership and Control*. Journal of Law and Economics 26: 301–326.

Freidank, C., Velte, P., & Weber, S. (2009). *The auditor as an element of in and external corporate governance*. Corporate Ownership, Journal of Management Control, Volume 23, Issue 1 , pp 81-91

Gamble, A. & Kelly, G. (2001). *Shareholder Value and the Stakeholder Debate in the UK*, *Corporate Governance: An International Review*, Vol. 9, No. 2: 110-7.

George N. (2005). *The Role of Audit Committees in the Public Sector*, The journal of CPA, August 2005 Issue

Giuseppina T, (2011). *Corporate governance and capital flows*, *Corporate Governance*, Vol. 11 Iss: 3pp. 228 – 243

Gompers, P., Ishii, J. & Metrick, A., (2003). *Corporate Governance and Equity Prices*. Quarterly Journal of Economics, 118, 107–155

Government of Kenya (2012). *Challenges Facing The Capital Markets*. Nairobi: Government Printer.

Grace, W. (2005). *Capital Markets in Emerging Economies: A case study of the Nairobi Stock Exchange*. Published master's thesis, The Fletcher School, Tufts University.

Hall, J. (1989). *The Nation-State in Transformation: The Governance, Growth and Cohesion of Small States*, University of Minnesota Press, pp. 1-125. Open University Press.

Henry, G. (2010). *Corporate Governance – Getting Back to Market Basics*

Henry, A. (2008). *Understanding Strategic Management*. Oxford University Press,

Hermalin, B. & Weisbach, M. (2003). *Boards of Directors as an Endogenously Determined Institution: A Survey of the Economic Literature*". *Economic Policy Review*, 9, 7–26

Jensen, M., & Meckling, W. (1976). Theory of Firm: managerial behavior, agency costs and Capital Structure. *Journal of Financial Economics*. Vol 2,(2),15 ?? page # range

Keasey, K. & Wright, M. (1993). *Issues in corporate accountability and governance*. Accounting and Business Research, Vol. 23, pp. 291-303.

Kenya Business Review (2012). *Kenya Business Review*, Nairobi. Available at:  
<http://businessreviewkenya.com/kenya-business-reviewprotecting-investors-in-kenya/>  
[accessed 10 February 2013]

La Porta, R., Lopez-de-Silanes, F., Shleifer, A., Vishny, R., (2000). *Investor Protection and Corporate Governance*. *Journal of Financial Economics* 58, 3–27.

Lang, W. & Jagtiani J, (2010). *Strategic default on first and second lien mortgages during the financial crisis*, Working Papers 11-3

Mellenbergh, G. J. (2008). Chapter 10: Tests and Questionnaires: Construction and administration. In Adèr, H.J., & Mellenbergh, G. J. (Eds.) *Advising on Research Methods: a consultant's opinion* (pp. 211--236). Huizen: Johannes van Kessel Publishing.

Monks, R. & Minnow N (2009). *Corporate Governance*. Malden, M.A: Blackwell Publishers.  
115

Mugenda, A.. (2008). *Social Science Research*. Nairobi: Acts Press.

Nicholas B. (2009). *The Impact of Uncertainty Shocks*. The Econometric Society

Nordin O. (2009). *Consumers attitude towards counterfeit products in Malaysia*: Faculty of Business and Accountability, University of Malaysia.

OECD (2004). Organization for Economic Cooperation and Development: *Principles of Corporate Governance*. OECD: Paris

Orodho, A., & Kombo, D. (2002). *Research methods*. Nairobi: Kenyatta University, Institute of Open Learning

O'Sullivan, N. & O'Dwyer, B. (2009). Stakeholder perspectives on a financial sector legitimating process: the case of NGOs and the equator principles, *Accounting, Auditing & Accountability Journal*, Vol. 22 No. 4, pp. 553-87

Patrick. F., Smith P. & Pharm. D. (2009). Types of Data: *Descriptive Statistics and Statistical Tests for Nominal Data*. University of Buffalo, Buffalo, New York.

Perry, T., & Shivdasani A., (2005). Do Boards Affect Performance? Evidence from Corporate Restructuring, *Journal of Business* 78, 1403–1432.

Petzold, K. & Nippa, M. (2005). Corporate Governance, Management Decision Making: Impacts of Justification Behavior, *The Costs of Corporate Governance*

Rosenstein, S., & Wyatt J., (1990). Outside Directors, Board Independence, and Shareholder Wealth, *Journal of Financial Economics* 26, 175-191.

Rousson, V., Gasser T. & Seifert B. (2002). Assessing intrarater, interrater and test-retest reliability of continuous measurements.

Ruppen, D. (2002). *Corporate Governance* bei Venture- Capital-finanzierten Unternehmen

Sacks O. (1997). *The Island of the Colorblind*. Knopf Doubleday Publishing Group

Saunders, M., Lewis P. & Thornhill, A. (2009). *Research methods for business students*,  
Financial Times/Prentice Hall

Statoil (2011). Statoil: *Human Resource Management International Digest*, vol. 19 no. 2, pp. 8-  
11, Emerald Group Publishing Limited

Strathmore (2013). Strathmore Business Schools, Available at:  
[www.strathmore.edu/News.php?NewsID=52](http://www.strathmore.edu/News.php?NewsID=52) [Accessed 10 February 2013]

Sullivan, D. & Conlon, D. (1997). *Crisis and Transition in Corporate Governance Paradigms:  
the Role of the Chancery Court of Delaware*, *Lawand Society Review*, 31, 713–763.

Tricker, R. (1984). *International Corporate Governance*. Cornell University Press, New York,  
NY.

Trochim, K., & William K. (2006). *Research Methods Knowledge*. Available at:  
[www.socialresearchmethods.net](http://www.socialresearchmethods.net) [Accessed 8 May 2013]

Vermeeren, (2006). *Reliability of a checklist-based user test data analysis*. In R.N Pikaar, EAP  
Koningsveld & PJM Settels (Eds.), *Proceedings IEA2006 Congress* (pp. 1-6).  
Amsterdam: Elsevier

Von W. (2003). *Corporate Governance & Shareholder Rights*, Berlin

Warren R.(2000). *Corporate Governance and Accountability*, Liverpool Academic Press,  
Bromborough.

Winyi, W. (2012). Solutions Kenya. Available at: <http://solutionskenya.wordpress.com/2012/02/>  
[Accessed 12 April 2013].

Winnie, N.. (2006). *Factors Affecting the Growth of SMES in Kenya: A case study of Ongata  
Rongai*. Unpublished Master's thesis, University of Nairobi. Nairobi.



## APPENDICES

### Appendix A - Timeline of Activities This can be removed.

Draft Title of Thesis: AN EXPLORATORY STUDY OF THE INFLUENCE OF CORPORATE GOVERNANCE MECHANISMS ON FIRM PERFORMANCE IN KENYAN STOCKBROKERAGE FIRMS

---

### WORK PLAN

Progress Stage	Stage Description	Proposed dates
1	Scoping of the Research study	
2	Choice of Research Topic	
3	Research Problem clarification, Research objectives, Purpose and Significance	
4	Foundation Literature survey	
5	Proposal of Research Methodology	
6	Advanced Literature Review (Chapter By Chapter)	
7	Detailed Proposal of Research Methodology	
8	Data Collection	
9	Data analysis and Interpretation	
10	Thesis Report writing	
11	Thesis Report Assessment By Supervisors	
12	Thesis Correction Upon Assessment By Supervisors	

Any remarks:

---

---

**Appendix B – Letter of introduction**

1<sup>st</sup> March, 2013

Strathmore Business School  
Nairobi.

Dear Respondent,

**RE: REQUEST TO FILL THE QUESTIONNAIRE**

I am an MBA student at Strathmore University, and I wish to undertake the study whose topic is  
“An Evaluation of Corporate Governance Mechanisms and their Implication on Firm Performance of Kenyan Stockbrokerage Firms”

I therefore kindly request that you take 10 minutes to respond to the questionnaire. This is an academic research and the information you provide will be used for academic purposes only and treated with confidence. Strict ethical principles will be observed to ensure confidentiality.

There will be no reference to your name or firm shop in the analysis; however I have provided my contacts and email address for any clarification. The response you provide will help in accomplishing the research objectives and will enable me complete my studies. The results will help in formulating policies that will support you.

In case of any questions, please do not hesitate to contact the undersigned. Thank you very much for your invaluable contribution and we appreciate the time you have spared to answer the questions.

Sincerely,

**Florence Kamau**

**0722852130**

## Appendix C - Research Instrument

Good morning/afternoon/evening. My name is ~, and I am conducting a study to evaluate the corporate governance mechanisms and their implication on firm performance of Kenyan stockbrokerage firms for a Thesis. I would appreciate your opinions. Please give answers in the spaces provided and tick (✓) in the box that matches your response to the questions where applicable

### PART A: DEMOGRAPHIC AND RESPONDENTS PROFILE

1) Name of the brokerage firm:.....

2) For how long has your firm been in existence?

a) Under 5 years ( ) c) 11 – 15 years ( )

b) 6 – 10 years ( ) d) Over 16 years ( )

3) What would you say is the ownership structure of the firm?

a) Locally owned ( ) c) Foreign Owned ( )

b) Foreign / Local ownership ( ) d) Government ownership ( )

4) Does your firm operate in other countries outside Kenya?

Yes ( )

No ( )

If yes, please give the countries that you operate in.....

5) Length of continuous service with the brokerage firm?

a) Less than five years ( ) c) 10 - 15 years ( )

b) 5 - 10 years ( ) d) Over 16 years ( )

6) What is your highest level of education?

a) Primary ( ) c) Middle level college ( )

- b) Secondary ( )                      d) University ( )

**PART B: Corporate Governance Policies and Practices**

**Section 1: The Board**

7) How many board members does your firm have? .....

8) Does the board have a fixed term?

- Yes ( )                      No ( )

If yes, how many years? .....

9) How are the board members, chairman of the board and the CEO of your organization appointed?

- a) Direct appointment by the owners ( )
- b) Through recruitment process ( )
- c) None of the above ( )

10) Would it make a difference if the process above were different? Please explain

.....  
.....

11) Do you think the membership of your firm board is diversified in terms of their background and skills?

- Yes ( )                      No ( )

Explain

.....  
.....

12) In a scale of 1-5, to what extent do you agree with the following statement concerning the organization's board? (Please Tick)

**KEY** 5) Strongly agree 4) Agree 3) Neutral 2) Disagree 1) Strongly disagree

Statement	5	4	3	2	1
The board members educational qualification is sufficient to carry out their duties in the firm					
The board members professional qualification is considered before appointment					
The board members action is independent from outside influence					
The independent directors proportion to the executive directors is as per the CMA guidelines					
The board members are honest and objectively accountable in their dealings					
The board ensures that the firm conforms to legislation and government policies as well as achieve agreed outcomes					
The frequency of the board meetings is adequate to determine policy decisions					
There exist adequate succession plan for the board members in the firm					

**Section 2: Audit Committee**

13) Does your organization have an Audit Committee?

Yes ( ) No ( )

14) If your answer to above is yes, please indicate the extent to which the following attributes associated with the audit committee exist.

Key      5) Very great extent      4) Great extent      3) Moderate extent      2) Little  
 Extent      1) Not at all

Statement	5	4	3	2	1
The audit committee is responsible for recommending external auditor					
Responsible for ensuring the soundness and quality of internal accounting and control practices of the firm					
Concerned with monitoring the external auditor's independence from senior management					
The frequency of meetings by the audit committee is considered to be adequate					
The organization has a well developed governance manual					

15) On a scale of 5 -1 (Range is from Most important to Least Important ), indicate the importance to which the firm places in each of the following factors influencing corporate governance practices

Practice	5	4	3	2	1
Audit Committee					
Directors Nomination committee					
Directors Compensation Committee					
Availability of code of conduct					

16) In a scale of 1-5, to what extent does the following elements of conformance and compliance do you perceive to be lacking in your organization? (Please Tick)

**Key** 5) Strongly agree    4) Agree    3) Neutral    2) Disagree    1) Strongly disagree

Element	5	4	3	2	1
Upholding the firms' values and ethics					
Guidance on policies, procedures, processes, principles and tasks					
Ensuring and maintaining confidentiality					
Enforcing security and fraud controls					
Compliance with legislative guidelines as required					
Quality assurance					

**Section 3: Code of Conduct**

17) Does your organization have a Code of Conduct?

Yes            (    )            No            (    )

18) If your answer to above is yes, please indicate the extent to which the following attributes associated with the Code of Conduct

Key            5) Very great extent    4) Great extent    3) Moderate extent    2) Little  
Extent    1) Not at all

Statement	5	4	3	2	1
The Code of Conduct is upheld by the Board and all staff					
Code of conduct is inculcated in job descriptions					
There are meetings with agenda on code of conduct					
The organization has a well developed code of conduct manual					

**Section 4: Conclusion**

19) How have the CMA rules introduced in 2011, been implemented in your stockbrokerage firm?

.....

.....

.....

20) What have been your challenges and experiences in seeking the implementing of CG policies and practices?

.....

.....

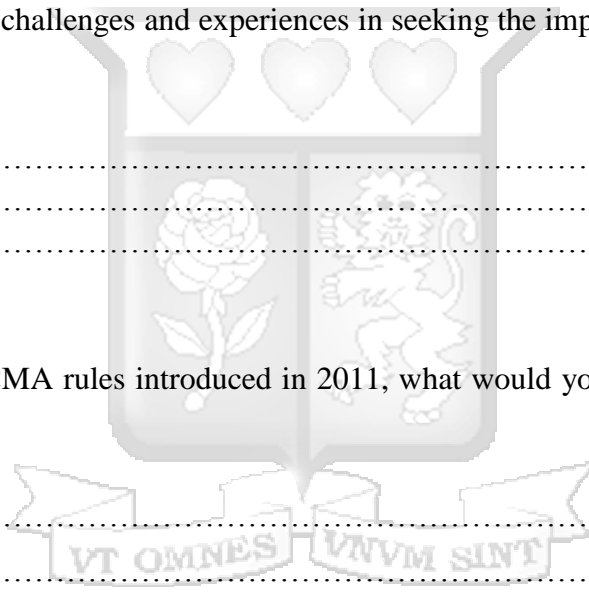
.....

21) With regards to the CMA rules introduced in 2011, what would you recommend as areas of improvement?

.....

.....

.....



## Appendix D – List of Stockbrokerage firms in Kenya

1	Afrika Investment Bank Ltd
2	ABC Capital Ltd
3	African Alliance (Kenya) Securities Ltd
4	Apex Africa Capital Ltd
5	CFC Stanbic House,
*6	Discount Securities Ltd
7	Drummond Investment Bank Limited
8	Dyer & Blair Investment Bank Ltd
9	Faida Investment Bank Ltd
10	Genghis Capital Ltd
11	Kestrel Capital (EA) Limited
12	Kingdom Securities Ltd
*13	Ngenye Kariuki & Co. Ltd
14	NIC Securities Limited
15	Reliable Securities Ltd
16	Renaissance Capital (Kenya) Ltd
17	Standard Investment Bank Ltd
18	Sterling Investment Bank Ltd
19	Suntra Investment Bank Ltd
*	Under Statutory Management

