

**RELATIONSHIP BETWEEN CORPORATE GOVERNANCE PRACTICES AND
FINANCIAL PERFORMANCE OF TEA FACTORIES IN KISII COUNTY,
KENYA**

BY

HASSAN MOMANYI

**A RESEARCH PROJECT SUBMITTED IN PARTIAL FULFILMENT FOR THE
REQUIREMENTS FOR THE DEGREE OF MASTER OF BUSINESS
ADMINISTRATION**

SCHOOL OF BUSINESS AND ECONOMICS

MASENO UNIVERSITY

© 2016

ABSTRACT

Tea farming contributes about 40% to agricultural export in Kenya. Despite the overall contribution, Kenya Tea Development Agency (KTDA) tea factories in Kisii County have continued to perform poorly leading to 5% of farmers exiting the industry for the period 2010 to 2015. Previous studies show that corporate governance practices influence financial performance of firms. However, the relationship between corporate governance practices and financial performance of the KTDA factories in Kisii County is unknown. The purpose of the study was to establish the relationship between corporate governance practices and financial performance of tea factories in Kisii County. Specific objectives were to; establish the relationship between board composition and financial performance of KTDA factories; establish the relationship between stakeholder involvement and financial performance of KTDA factories; and to assess the relationship between audit committees and financial performance of KTDA factories in Kisii County. The study was guided by the stakeholder theory and correlational research design. Out of a population of 50 respondents, a saturated sample of 40 was taken. A pre-test of 10 questionnaires was conducted. Reliability coefficient of 0.83 and content validity index (CVI) of 0.79 were computed. The results were above the threshold of 0.7 indicating that the data collection instrument was valid and reliable. Primary data were from Questionnaires while secondary data were from the factories' documents. Correlation and multiple regression analysis were used to analyse the relationship between the corporate governance practices and financial performance of the tea factories. The study revealed that stakeholder involvement ($B= 0.293, p= 0.007$) and audit committee ($B= 0.381, p= 0.034$) both had positive and significant influence on financial performance while board composition had insignificant positive influence on financial performance of the tea factories. This implies that when stakeholders are involved in decision making, financial performance will significantly increase by 0.293. Similarly when audit committee is involved in decision making, financial performance of the tea factories will significantly increase by 0.381. The study concludes that Boards composition and audit committee significantly influence financial performance of KTDA factories in Kisii County. The study thus recommends that there should be continued involvement of audit committees and stakeholders in decision making to enhance financial performance. The study findings may be helpful to decision makers in the tea industry and provide literature for academia.

CHAPTER ONE

INTRODUCTION

This chapter presents an overview of the concept of corporate governance as a strategy that is gaining ground in firms in Kenya and more specifically the tea industry. It also presents the research problem, the objectives of the study, the research questions, justification of the study and the conceptual framework that the researcher adopted.

1.1 Background to the Study

As posited by Ramon (2001), it is difficult to define the concept of corporate governance in a universally acceptable way but generally, it is agreed that the following elements are key pointers in corporate governance: stakeholder involvement which require that firms should respect the rights of shareholders and other stakeholders through effective communication of information; interests of other stakeholders which calls for a firm to note and appreciate other non-shareholder stakeholders; role and responsibility of the board calling for effort to ensure that the board has relevant and sufficient skills to review and challenge management performance; integrity and ethical behavior and disclosure and transparency where an organization is expected to uphold integrity while choosing employees and board members and finally disclosure and transparency through audit committees which puts a burden upon organizations to clarify and make publicly known the financial matters of the firms so as to provide stakeholders with a level of accountability.

According to a World Bank (1999) report, corporate governance comprises two mechanisms; internal and external corporate governance. Internal corporate governance involves giving priority to shareholders' interests and operating on the board of directors to monitor top management. On the other hand, external corporate governance monitors and controls managers' behaviors by means of external regulations and forces, in which many parties are involved such as suppliers, debtors (stakeholders), accountants, lawyers, providers of credit ratings and professional institutions.

Bauer *et al.* (2007) note that empirical research has shown significant relationships between various corporate governance features and corporate financial performance.

However, majority of researchers have focused on specific features of corporate governance, which makes it difficult to establish an overall relationship between corporate governance and corporate performance. According to Bauer *et al* (2007), relating corporate performance to a particular aspect of corporate governance may not capture the true relationship unless that specific aspect is controlled for other aspects of governance. A number of developing countries, including Kenya, have embraced the corporate governance ideals. However, developing countries practice corporate governance models that are different from the models adopted by developed countries (Rabelo, 2002). This is partly due to the unique economic and political systems found in developing countries. Mensah (2002) argues that developing countries are poorly equipped to implement the type of corporate governance found in the developed market economies because developing countries are characterized by state ownership of firms, interlocking relationships between governments and financial sectors, weak legal and judiciary systems and limited human resource capabilities.

According to Reed (2002), the problem with corporate governance in Africa is that corporate governance structures in developing countries are weak. Consequently, several measures have been suggested on how to improve such structures. Notable suggestions include the use of equity instead of debt for growth, increasing overall investor confidence through increased transparency, strengthening of capital market structures and encouraging the use of competition to improve performance of domestic firms. However, there is a general agreement that the best way to improve governance is by strengthening corporate governance principles of board composition, stakeholder involvement and the role of audit committees. Empirical research on these principles has however indicated that the relationship between them and financial performance is not clear.

Studies that have been conducted on the role of board composition on performance of firms have brought out conflicting results. Hypothetically, when a board is composed of people with varied skills and experiences, the performance of the firm is supposedly thought to improve. This is because the synergy between the skills and experiences should help improve the performance of the firm. For example, Muchiri (2010) in his study on the impact of corporate governance in schools in Kenya found that schools with

mixed board structures were better in financial performance. However, the study does not indicate whether the influence of board structure on financial performance is significant. Furthermore, schools are not profit-oriented meaning that the relationship between board composition and financial performance was not established. In a differing study, Young (2011) in a study of corporate governance strategy in listed firms in Asian countries found a negative significant relationship between the proportion of external directors and firm performance. However, the study's findings cannot be generalised since the study was conducted among listed companies in Asian countries whose corporate governance practices are regulated by the securities market authorities.

Oketch (2004) conducted a study on the role board structure in corporate performance for the United Nations Development Programme (UNDP). The study found that board structure as a corporate governance practice plays a significant positive role in the performance of firms. In another study in Kenya by Kaptein (2003), who studied the role of boards across several institutions in Kenya using a correlational design, it was found that if the board is truly to hold corporate managers accountable to shareholder interests, the members of the board must genuinely represent shareholders rather than management. It was therefore concluded that board composition in terms of knowledge had a significant positive relationship with performance. Chukwuemeka *et al.*, (2011), conducted a study on the effect of corporate governance practices on the performance of government organizations using Enugu State of Nigeria as a case in study. The findings of the study revealed among others that there is a negative relationship between board composition and the performance of corporate governance regulatory agencies.

The review of empirical literature shows that there is a possibility of board structure influencing financial performance of firms. Muchiri (2010), Oketch (2004) and Kaptein (2003) find a positive relationship between board composition and performance of firms while Young's (2011) and Chukwuemeka's (2011) findings differ by indicating a negative relationship between the variables. Furthermore, the study by Muchiri (2010) does not indicate the significance of the relationship. The conflicting results arise due to the different methodologies used and the contexts. For instance uses a sample from public secondary schools which are non-profit oriented. Oketch studies a non-governmental

organization while Chukwuemeka *et al.* (2011) studies public institutions in Nigeria. This implies that no studies have used similar data implying that the results cannot be generalized. It is evident therefore that there are no known studies that have been conducted to establish the relationship of board composition and financial performance of KTDA factories in Kisii County.

The role of stakeholder involvement on the financial performance of firms has not been established with certainty as proven from empirical literature. Akodoh (2012) conducted a study in Uganda on the relationship between corporate governance and financial performance in four public universities using a cross sectional and correlational design revealed that corporate governance practices were on the increase in African countries and that stakeholder involvement in decision making had a significant positive relationship with financial performance. In contrary findings, Wu *et al.* (2013) conducted a study on effects of corporate governance on firm performance in China's listed companies while employing return on assets, stock return and Tobin's Q in the study to measure firm performance. The empirical results indicated that firm performance is in negative and significant relation stakeholder involvement. Miringu (2012) conducted a study on an analysis of the effect of corporate governance on performance of commercial state corporations in Kenya found that the level of respect for stakeholders in state corporations was high and that there is a positive relationship between stakeholder management and performance of all state corporations involved in the study. Rwegasira (2000) conducted a study on the influence of corporate governance in government institutions in Kenya using a survey design found no significant relationship between stakeholder management and performance of firms. Mensah (2002) found no relationship between shareholder's rights and performance in a study on corporate governance in Nigeria focusing on the role of accounting in corporate governance.

From the reviewed studies above on the relationship between stakeholder involvement and performance of firms have indicated conflicting results that however show a possibility of stakeholder involvement influencing financial performance of firms. However, the study findings cannot be generalised since different methodologies were used. For example, Miringu (2012) studied commercial state corporations using a survey

research design which does not establish cause-effect relationships. Akodoh (2012) studied public universities in Uganda which are not profit-oriented and therefore the results from the study cannot be generalised to profit-oriented institutions such as KTDA factories. Wu *et al.* (2013) studied listed firms in China which is a developed country. General findings indicate however that while some studies find a positive significant relationship (Akodoh, 2012; Miringu, 2012) others find a negative significant relationship (Wu *et al.*, 2013) while Rwegasira (2000) and Mensah (2002) find no relationship between the variables. Since no studies have been conducted using the same sample, it is therefore clear that no known study has been conducted to establish the relationship between stakeholder involvement and financial performance of KTDA factories in Kisii County indicating that the relationship between stakeholder involvement and financial performance of KTDA factories in Kisii County is unknown.

Audit committees are identified as effective means for corporate governance that reduce the potential for fraudulent financial reporting (Al-Baidhani, 2014). Audit committees oversee the organization's management, internal and external auditors to protect and preserve the shareholders' equity and interests. To ensure effective corporate governance, the audit committee report should be included annually in the organization's proxy statement, stating whether the audit committee has reviewed and discussed the financial statements with the management and the internal auditors. Ramon (2001) notes that the audit committee operates as a representative of the board of directors from whom it receives its powers to perform its corporate governance responsibilities which include overseeing and monitoring the organization's financial reporting, disclosure, internal and external audit, internal control, regulatory compliance, and risk management activities; this applies to public, private, and mix sectors, as well as some non-governmental and not-for profit organizations. The audit committee provides the board of directors with necessary advices and recommendations which include ensuring: that the respective organization complies with relevant regulations and ethical principles and standards; that the internal auditors are independent and competent; that the financial statements have been prepared correctly and accurately; and that the compensations paid to the organization's executives are according to fairness and professionalism.

Empirical studies on the role of audit committees on performance of organizations have also produced mixed results. Al-Baidhani (2014) while studying the role of audit committees on the performance of firms, the board of directors and its committees, including the audit committee found that firms which had strong audit committees were better in performance as opposed to those which didn't have. The results indicated a significant positive influence. In a research by Ojeka *et al.*, (2014) on the effectiveness of audit committee and firm financial performance in Nigeria using a sample of 25 firms, it was found that certain measures of audit committee effectiveness such as audit committee independence, audit committee financial expertise and board size have positive coefficients and significantly influence the firm's financial performance. Al-Memun *et al.*, (2014) studied the relationship between audit committee characteristics and economic value added of public listed companies in Malaysia using 32 Sarawak based companies listed in the Bursa Malaysia from 2008 to 2010 found significant association between audit committee characteristics and firm performance and also with audit quality. However, the study reports that not all the audit committee characteristics are associated with firm performance. For instance, meeting frequency and accounting and financial expertise of audit committee members do not possess any influence on firm performance. In similar findings, Ogoro and Simiyu (2015) studied the relationship between the characteristics of audit committees and its effectiveness in reducing the number of financial statement restatements for State Corporations in Kenya found that the most important and influential characteristics of audit committees is multiple directorships and audit committee tenure as they are statistically significant in reducing the number of financial statements.

Although most of the reviewed studies seem to agree that audit committees have a positive relationship with firm performance, it is evident that the degree of this influence varies among the studies. Furthermore, the reviewed studies use different methodologies which may have limited generalization of the findings. Al-Memun *et al.*, (2014) study listed firms in Malaysia whose corporate governance practices are regulated by security markets. Ogoro and Simiyu (2015) study state corporations in Kenya most of which are non-profit oriented. Al-Baidhani studies firms in Nigeria using a survey study design indicating that the significance of the relationship between audit committee and financial

performance of the firms was not established with statistical accuracy. It is therefore evident that specific studies on the relationship between audit committees and financial performance of KTDA factories are missing.

Researchers studying management have recommended multiple measures of firm performance. These measures are broadly classified into financial, social and economic. Singh (2003) asserts that three measures of organizational performance namely, return on assets indicating profitability, growth in sales indicating how well customers accept the firm's products or services, and price cost margin can be used to measure performance. Paul and Anantharaman (2003) measured organizational performance along two dimensions: operational and financial. Operational performance was defined in terms of employee retention, employee productivity, product quality, speed of delivery, and operating cost. Financial performance was measured in terms of growth in sales, net profit, and return on investment.

How best a firm is performing can be looked at in terms of profitability and rate of return. Financial performance measures the results of a firm's policies and operations in monetary terms. In tea factories, it is the return to the tea farmers in terms of the monthly pay which is pegged on their tea harvest, and the return in terms of bonuses which are earned from the sales of the tea in the world markets. The performance of the tea factories in terms of the annual bonus differs from factory to factory.

According to Richard *et al.* (2009) organizational performance encompasses three specific areas of firm outcomes: financial performance (profits, return on assets, return on investment, etc.); product market performance (sales, market share, etc.); and shareholder return (total shareholder return, economic value added, etc.) On the other hand, firm performance can also be measured using perceived performance approach (also referred to as subjective performance measure) where Likert-like scaling is used to measure firm performance from the top management perspectives (Selvarajan, 2007).

Organizational performance is a method of measuring the success of the organization to ensure that it achieves its goals. The success of an organization is gauged from several indicators both qualitative and quantitative (Fry *et al.*, 2008). These include financial

performance and nonfinancial performance. Performance measures may be cost-oriented or non-cost oriented and can be internal or external.

Performance has been traditionally conceptualized in terms of financial measures; but some scholars have proposed a broader performance construct that incorporates non-financial measures including among others market share, product quality, and company image. Financial measures of performance are criticized for lacking neutrality (Emmanuel *et al.*, 1990); and encouraging short-termism (Wilson & Chau, 1993). Most management practices built around financial measures bear little relation to a company's progress in achieving long term objectives. Financial measures are also criticized for lacking balance because they are more concerned with physical assets and ignore, for instance, perspectives of customers, and internal business processes. All these perspectives are necessary under the circumstances where companies transform themselves for competition based on information.

Under the circumstances, non-financial measures of performance have also been used to gauge the performance of a firm (Kaplan & Norton, 2009). Some studies (Youndt *et al.*, 2006) suggest asking managers to assess their own firm's performance relative to others in the same industry or sector. They suggest the use of multiple items and multiple respondents to assess performance. This study opts to use the financial measure of performance in order to assess the performance of the organizations under study, by using profits, return on assets, and return on investment. This is because these measures are measurable.

Statistics indicate that tea contributes about 40% to agricultural export of Kenya out of which almost 60% is from small-scale tea farmers who are managed by the Kenya Tea Development Agency (KTDA). The Kenya Tea Development Agency (KTDA) factory network has 66 tea processing factories owned by 54 factory companies. The factories have been divided into seven regions. About 560,000 small scale tea farmers supply Green leaf to the respective tea processing factories. The farmers are shareholders in the factories, (KTDA, 2014). According to KTDA (2014), the agency works with tea factories to manage costs, by offering extension services to the farmers on their tea farms, manage tea production processes and invest prudently in order to secure the farmers'

financial future. This is demonstrated by the fact that all KTDA managed tea factories have been ISO: 9001:2008 certified for efficient management systems while more than 90% of the factories have attained the more comprehensive ISO 22000:2005 for Food Safety Management System.

Tea factories in Kisii County are in Region six (KTDA, 2014). There are seven tea factories in Kisii County, namely; Ogembo, Nyankoba, Nyamache, Kiamokama, Itumbe, Eberege, and Rianyamwamu (KTDA, 2014), with the last three being satellite factories of Nyamache, Ogembo and Kiamokama respectively. Statistics available from KTDA indicates that tea factories in this region have been performing poorly in the annual bonus payout. In the year 2011/2012, when the average country average annual bonus payout was Ksh. 48, Ogembo, Nyankoba, Nyamache, Itumbe and Kiamokama received Ksh. 42, Ksh. 42.50, Ksh. 41.50, Ksh. 43 and Ksh. 42.55 respectively. In the financial year 2013/2014, the payout fell to Ksh. 22.50, Ksh. 24.50, Ksh. 23.50, Ksh. 26 and Ksh. 25.00 respectively, when the national average was Ksh. 31. It was noted that in the last year, Ogembo was the lowest payer among the 65 affiliated factory companies. The low morale from tea farmers has led to a reduced number of new farmers. Statistics indicate that 5 % of tea farmers in Kisii County have exited from tea farming in the period 2010 to 2014 (KTDA, 2014). Several studies have been conducted on KTDA and especially on the performance of the agency indicate poor financial performance. However, most of these studies have concentrated on general aspects of performance of the Agency in relation to managerial practices. Specific studies relating corporate governance and financial performance of KTDA are scanty.

1.2 Statement of the Problem

Tea is the main cash crop in Kisii County with statistics indicating that the crop contributes about 40% to agricultural export in Kenya. However, there is empirical evidence that the Kenyan tea industry is struggling to survive with the problem being more prevalent in Kisii County where tea farmers are demoralized by constantly receiving the lowest rates in the annual bonus payment. This is supported by the fact that there are about 5% old farmers who have exited the industry an indication that tea farming is no longer an attractive venture, a problem attributed to poor financial

performance in the factories. Empirical studies link corporate governance to financial performance. However, no known study has been conducted to establish the relationship between stakeholder involvement and financial performance of KTDA factories in Kisii County indicating that the relationship between stakeholder involvement and financial performance of KTDA factories in Kisii County is unknown. Empirical evidence also shows that no known study has been conducted to establish the relationship between stakeholder involvement and financial performance of KTDA factories in Kisii County. Similarly, there is no study that has attempted to assess the relationship between audit committees and financial performance of KTDA factories. It was therefore evident that generally the relationship between corporate governance practices and financial performance of KTDA factories has not been established.

1.3 Research Objectives

1.3.1 General Objective

The study sought to establish the relationship between corporate governance practices and financial performance of tea factories in Kisii County, Kenya.

1.3.2 Specific Objectives

Specifically, the study sought to:

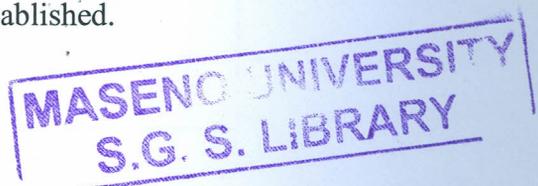
- (i) Establish the relationship between Boards composition and financial performance of KTDA factories in Kisii County.
- (ii) Determine the relationship between stakeholder involvement and financial performance of KTDA factories in Kisii County.
- (iii) Asses the relationship between audit committees and financial performance of KTDA factories in Kisii County.

1.4 Research Hypotheses

This research was guided by the research hypotheses stated below:

H₀1: There is no relationship between board composition and financial performance of KTDA factories in Kisii County.

H₀2: There is no relationship between stakeholder involvement and financial performance of KTDA factories in Kisii County.



CHAPTER TWO LITERATURE REVIEW

This chapter reviews the theoretical and empirical literature on the key study variables. This review was intended to identify the research gaps. The literature review more precisely examines the existing literature on corporate governance practices and financial performance.

2.1 Theoretical Perspectives

According to Salacuse (2009), the term corporate governance appears to have arisen and entered into prominent usage in the mid-to-late 1970's in the United States in the wake of the Watergate scandal and the discovery that major American corporations had engaged in secret political contributions and corrupt payments abroad. Eventually it also gained currency in the rest of the world as a concept distinct from corporate management, company law or corporate organization (Salacuse, 2009).

Scholars and practitioners of corporate governance give the term a wide variety of definitions. Economists and social scientists tend to define it broadly as the institutions that influence how business corporations allocate resources and returns and the organizations and rules that affect expectations about the exercise of control of resources in firms. These definitions focus not only on the formal rules and institutions of corporate governance, but also on the informal practices that evolve in the absence or weakness of formal rules. Moreover, they encompass not only the internal structure of the corporation but also its external environment, including capital and labour markets, bankruptcy systems, and government competition policies, (Salacuse, 2009)

The United Kingdom's 1992 Cadbury Report's often quoted definition of Corporate Governance is that corporate governance is the system by which businesses are directed and controlled. As applied in practice, this definition focuses almost exclusively on the internal structure and operation of the corporation's decision-making processes. It is this definition that has been central to public policy discussions about corporate governance in most countries. The OECD Principles of Corporate Governance deal with five topical areas: The Rights of Shareholders; The Equitable Treatment of Shareholders; the Role of Stakeholders in Corporate Governance; Disclosure and Transparency; and the

Responsibility of the Board (OECD, 2011). According to Maherm and Anderson, (1999) there are basically two different models that explain the corporation, the shareholder model and the stakeholder model.

2.1.1 The Shareholder theory

According to Reed (2001), shareholder theory indicates that the objective of the firm is to maximize shareholder wealth through allocative, productive and dynamic efficiency i.e. the objective of the firm is to maximize profits. The criteria by which performance is judged in this model can simply be taken as the market value (i.e. shareholder value) of the firm. Therefore, managers and directors have an implicit obligation to ensure that firms are run in the interests of shareholders. The underlying problem of corporate governance in this model stems from the principal-agent relationship arising from the separation of beneficial ownership and executive decision-making. It is this separation that causes the firm's behaviour to diverge from the profit maximizing ideal. This happens because the interests and objectives of the principal (the investors) and the agent (the managers) differ when there is a separation of ownership and control. Since the managers are not the owners of the firm they do not bear the full costs, or reap the full benefits, of their actions. Therefore, although investors are interested in maximizing shareholder value, managers may have other objectives such as maximizing their salaries, growth in market share, and an attachment to particular investment projects. The major weakness of this theory is that it only focus on the shareholders welfare hence it does not give a whole picture of the industry.

2.1.2 The Stakeholder Theory

This theory was advanced by Blair (1995). The stakeholder theory takes a broader view of the firm. The theory views the corporation as being responsible to a wider constituency of stakeholders other than shareholders. Other stakeholders may include contractual partners such as employees, suppliers, customers, creditors, and social constituents such as members of the community in which the firm is located, environmental interests, local and national governments, and society at large. This view holds that corporations should be "socially responsible" institutions, managed in the public interest. According to this model performance is judged by a wider constituency interested in employment, market

share, and growth in trading relations with suppliers and purchasers, as well as financial performance. This is the theory that this study will be anchored upon because it touches on all aspects of the industry.

2.13: Concept of Corporate Governance practices

Corporate Governance is a mechanism through which boards and directors are able to direct, monitor and supervise the conduct and operation of the corporation and its management in a manner that ensures appropriate levels of authority, accountability, stewardship, leadership, direction and control. Corporate governance codes do not often explicitly define what corporate governance is. Most codes of best practice deal with corporate governance as a concept and explain its importance without defining its meaning. Yet the way corporate governance is defined may affect the scope and content of a code. Perhaps the most famous definition of corporate governance was provided in 1992 by Sir Adrian Cadbury in the Report on Financial Aspects of Corporate Governance in the United Kingdom which states that corporate governance is concerned with holding the balance between economic and social goals and between individual and communal goal. The aim is to align as nearly as possible the interests of individuals, corporations and society. (Yoga, 2006).

A report by Hampel Committee (1998), on the other hand indicates that corporate governance is the system by which companies are directed and controlled. It can therefore be considered as a set of mechanisms through which firms operate when ownership is separated from management. But whether a broad or a narrow definition of corporate governance is chosen, it is important that the fundamental values of transparency, accountability, fairness, and responsibility be respected in order for firms to build and sustain the confidence of investors, stakeholders, and society as a whole. The importance of corporate governance lies in its contribution both to business prosperity and to accountability (Hampel Committee, 1998).

Similarly Murthy (2003) noted that corporate governance is susceptible both to broad and narrow definitions. The important point is that corporate governance is a concept, rather than an individual instrument. It includes debate on the appropriate management and control structures of a firm. Further it includes the rules relating to the power relations

between owners, the Board of Directors, management and, last but not least, the stakeholders such as employees, suppliers, customers and the public at large.

2.1.4 The concept of Financial Performance and its Constructs

The question of the firm performance is very important for different groups of people. All agents that have to make any financial decisions about a company are concerned with its financial position. Thus, owners, managers, potential investors, banks, other financial institutions, creditors, business partners, employees, and government are interested in models that help to analyse and predict the performance of the companies (Jonathan 1994).

Management researchers prefer accounting variables as performance measures such as return on equity (ROE), return on investment (ROI), and return on assets (ROA), along with their variability as measures of risk. Earlier studies typically measure accounting rates of return. These include: (ROI), return on capital (ROC), return on assets (ROA) and return on sales (ROS) (Hendrik and Elaine 2009).

The reason behind these measures is to evaluate managerial performance. Some of the problems with these measures are in public domain. For instance, Accounting returns include depreciation and inventory costs and affect the accurate reporting of earnings. Asset values are also recorded historically. Since accounting conventions make these variables unreliable, financial analysts prefer market returns or discounted cash flows as measures of performance. For the sake of consistency, two accounting measures ROE and ROA can be used along with market return to measure performance (Spong & Richard 2007). Return on equity (ROE) is a frequently used variable in judging top management performance, and for making executive compensation decisions. ROE can be used as a measure to judge performance and calculate the average return on equity (AROE) across all sampled firms and time periods, its standard deviation and also the coefficient of variation for each of the three diversification groups. ROE is defined as net income (income available to common stockholders) divided by stockholders equity. The coefficient of variation (CV) gives us the risk per unit of average return (Jonathan 1994). ROA is the most frequently used performance measure in previous studies. It is defined

as net income (income available to common stockholders), divided by the book value of total assets. We also calculate the average return on assets (AROA) across all sampled firms and time periods calculate its standard deviation and also the coefficient of variation for each of the three diversification groups (Hendrik and Elaine. 2009).

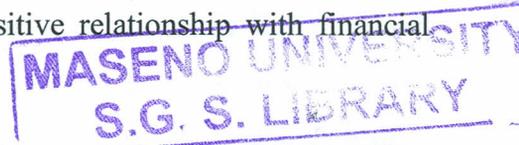
Generally good corporate governance enhances a firm's. In spite of the generally accepted notion that effective corporate governance enhances firm performance, other studies have reported negative relationship between corporate governance and firm performance (Hutchinson, 2002) or have not found any relationship (Davidson, 2003). Several explanations have been given to account for these inconsistencies. Some have argued that the problem lies in the use of either publicly available data or survey data as these sources are generally restricted in scope. It has also been pointed out that the nature of performance measures (i.e. restrictive use of accounting based measures such as return on assets (ROA), return on equity (ROE), return on capital employed (ROCE) or restrictive use of market based measures (such as market value of equities) could also contribute to this inconsistency (Gani and Jermias, 2006). Furthermore, it has been argued that the "theoretical and empirical literature in corporate governance considers the relationship between corporate performance and ownership or structure of boards of directors mostly using only two of these variables at a time" (Krivogorsky, 2006). To address some of the aforementioned problems, a look at corporate governance and its association with firm performance should take a multivariate approach.

2.2 Empirical Literature Review

2.2.1 Stakeholder Involvement and Performance

A number of studies have been conducted to investigate the relationship between stakeholders' management and performance. Most of these studies note that stakeholder management has an influence on the performance of firms. However, other studies find no such relationship. For instance, Akodoh (2012) conducted a study in Uganda on the relationship between corporate governance and financial performance in four public universities. The study was prompted by institutional turbulences as a result of adhoc policy and decision making processes and poor financial performance of public

universities. The study was aimed at establishing the relationship between corporate governance principles of board effectiveness and stakeholder participation and financial Performance of Public Universities. A cross sectional and correlational study was conducted in four public Universities in Uganda. The findings revealed that corporate governance practices were on the increase in African countries and that stakeholder involvement in decision making had a significant positive relationship with financial performance.



Wu *et al.* (2013) conducted a study on effects of corporate governance on firm performance in China's listed companies. The main purpose of the study was to examine the impact of the corporate governance mechanisms of board independence, insider ownership and stakeholder involvement on firm performance using a survey research design. The variables, employed in the study to measure firm performance were return on assets, stock return and Tobin's Q. The empirical results indicated that firm performance is in negative and significant relation to board size, CEO duality, stock pledge ratio and deviation between voting right and cash flow right. On the other hand, firm performance was found to be in positive and significant relation to board independence, insider ownership and stakeholder involvement.

Miringu (2012) conducted a study on an analysis of the effect of corporate governance on performance of commercial state corporations in Kenya. This study sought to examine how Corporate Governance affects performance in commercial state corporations in Kenya using a survey design. The study was prompted by the discovery that mismanagement, bureaucracy, wastage, incompetence and irresponsibility by directors and employees were the main problems that have made State corporations fail to achieve their performance. The target population for this study was 41 commercial state corporations in Kenya. The study found that the level of respect for stakeholders in state corporations was high and that there is a positive relationship between stakeholder management and performance of all state corporations involved in the study. The study recommended that all stakeholders should be involved in decision-making for organizations to perform well. The study was however focused on performance in general as opposed to the present study will be focused on financial performance.

Rwegasira (2000) while carrying out a research on the influence of corporate governance in government institutions in Kenya using a survey design found no significant relationship between stakeholder management and performance of firms. The study found further that the rules and institutions of corporate governance come from a wide variety of sources, both public and private, and mainly legislation. This legislation governs the creation, basic structure and primary rules of operation of the company, corporation, or other corporate legal form that a firm chooses to take. It also states some of the basic rights of shareholders, including the right to vote, to receive information about company matters, and to challenge management decisions in court.

Mensah (2002) conducted a study on corporate governance in Nigeria focusing on the role of accounting in corporate governance. Using a sample of 42 state corporations, the study used the stakeholders' management theory. The study was mainly descriptive in nature. The findings of the study were that accounting plays a vital role in corporate governance because it is fundamental to any disclosure regime concerning information about companies' activities to stakeholders. The study also found that a strong disclosure regime is essential for the exercise of shareholder rights, for the monitoring of corporations, and for imposing discipline on management. The study however found no relationship between shareholder's rights and performance. The study differs from the present study since it was conducted in another country and only used stakeholders as the dependent variable.

From the studies reviewed above, it is evident that the role of stakeholder involvement on the financial performance of firms has not been established with certainty. While Akodoh (2012), Miringu (2012), and Wu *et al.* (2013) find a significant positive relationship between stakeholder involvement and performance of firms, findings from their studies were in contradiction with those of Mensah (2012) and Rwegasira (2000) who found no significant relationship between stakeholder involvement and performance. Of the studies reviewed only Akodoh (2012) used correlational research design with the other studies either using survey or descriptive designs which are not confirmatory. It is also evident that the studies have mainly concentrated on state corporations (Miringu (2012); Mensah (2002); Akodoh (2012) and Rwegasira (2000)). It is therefore clear that no study has been

conducted to establish the relationship between stakeholder involvement and financial performance of KTDA factories in Kisii County.

2.2.2 Board Composition and Performance

Studies on corporate governance practices using board composition have found differing findings on the relationship between board composition and performance of firms. Muchiri (2010) conducted a study on the impact of corporate governance in schools in Kenya with particular reference to financial and academic performance. The focus of the study was on whether schools in Kenya had internalized board management strategy. His study was conducted among public secondary schools and it used descriptive statistical analysis tools to analyze the data. The study also found that boards were taking a greater role in corporate governance in schools. On the role of board composition on the performance of the schools, the study found that schools with mixed board structures were better in financial performance although the influence was not significant. This implies that board composition does not have a significant relationship with financial performance of schools.

Young (2011) in a study of corporate governance strategy in listed companies in Asia found a negative relationship between the proportion of external directors and firm performance. The research, which was correlational in nature, found that companies with more independent boards do not perform better than those companies with less independent boards. The findings suggest that it is unlikely that board composition and roles has a direct impact on firm performance. The effectiveness of any board is reflected on how well the board undertakes its performance and conformance role.

Oketch (2004) conducted a study on the role of the boards in corporate performance for the UNDP. The study which used financial performance as a measure for corporate performance using a survey design found that in varying degrees, all systems of corporate governance of publicly traded companies give the board a central position of responsibility. Although the board has certain key managerial tasks, such as selecting and removing the company's chief executive officer and approving important transactions, the fundamental task of the board in a publicly traded corporation is oversight of the

corporation's managers. The study found that boards play a significant role in the financial performance of firms.

In the study by Kaptein (2003), who studied the role of boards across several institutions in Kenya using a correlational design, it was found that if the board is truly to hold corporate managers accountable to shareholder interests, the members of the board must genuinely represent shareholders rather than management. Directors, although being elected by shareholders, management controls the voting process and chooses a single slate of nominees, most of whom are managers or have close relations with them. The study found that in recent years, good corporate practice has stressed measures to give corporate boards greater independence from management in the hope that the board would, as a result, represent shareholder interests more vigorously. It was therefore concluded that board composition in terms of knowledge had a significant positive relationship with financial performance of firms.

Chukwuemeka *et al.*, (2011), conducted a study on the effect of corporate governance practices on the performance of government organizations using Enugu State of Nigeria as a case in study. Twenty government establishments in Enugu were studied. Data was collected through questionnaire and face to face interview. The hypotheses were tested were tested using the Spearman's rank correlation. The findings of the study revealed among others that there is a significant negative relationship between board composition and the performance of corporate governance regulatory agencies. The study also found that corporate governance mechanism in Enugu state public organizations do not conform to the laid down standards.

It is apparent that the role of board composition on financial performance has not been agreed upon by scholars. Whereas Muchiri (2010) and Young (2001) find no significant relationship between board composition and performance of firms, the study by Oketch (2004). Kaptein (2003) and Chukwuemeka's (2011) find that board composition does influence financial performance of firms positively and significantly so. The methodologies used in the studies are also wanting since most of them were surveys. The studies were also concentrated in public listed companies. From the analysis, it is evident

that there are no studies that have been carried to establish the relationship of board composition and financial performance of KTDA factories in Kisii County.

2.2.3 Audit Committee and Performance

Empirical studies on whether audit committees have a role on performance of firms have also indicated varying findings with some studies finding a positive relationship and others a negative relationship. According to Al-Baidhani (2014) who studied the role of audit committees on the performance of firms, the board of directors and its committees, including the audit committee, rely on the organization's management to run the daily operations. The audit committee activities and responsibilities are to oversee and monitor the organization's overall financial performance, especially the preparation of its financial statements, managerial financial reports such as cost and budgeting reports, the effectiveness and efficiency of the organization's internal control, and the performance of both internal and external auditors. The study found that firms which had strong audit committees were better in performance as opposed to those which didn't have. However, the study did not indicate the extent to which the availability of the committees influence performance and especially financial performance.

In a study by Ojeka *et al.*, (2014) on the effectiveness of audit committee and firm financial performance in Nigeria using a sample of 25 firms, it was found that certain measures of audit committee effectiveness such as audit committee independence, audit committee financial expertise and board size have positive coefficients and significantly influence the firm's financial performance. Although, the result showed that audit committee meeting had a significant positive relationship with return on capital employed (ROCE), but generally the result showed that audit committee size and audit committee meeting did not add value to the firm's financial performance in Nigeria. The study concluded that audit committee members with financial expertise and the independence of the members do contribute significantly to the financial performance of firms.

Al-Memun *et al.*, (2014) studied the relationship between audit committee characteristics and economic value added of public listed companies in Malaysia using 32 Sarawak based companies listed in the Bursa Malaysia. The years from 2008 to 2010 were selected. The study found significant association between audit committee characteristics and firm

performance and also with audit quality. However, the study reports that not all the audit committee characteristics are associated with firm performance. For instance, meeting frequency and accounting and financial expertise of audit committee members do not possess any influence on firm performance.

Ogoro and Simiyu (2015) studied the relationship between the characteristics of audit committees and its effectiveness in reducing the number of financial statement restatements for State Corporations in Kenya. It used the following six characteristics of audit committees: independence of directors, committee size, meeting frequency, financial expertise, tenure and multiple directorships for 177 State corporations. The finance theory of agency was used as the theoretical underpinning for the study. The aim was to provide answers to two main research objectives by the use of cross sectional secondary data collected from the audited financial statements of the 177 State corporations in Kenya. The logistic regression model was used to test the effect of the characteristics of the committee on its effectiveness. The findings indicate that the most important and influential characteristics of audit committees is multiple directorships and audit committee tenure as they are statistically significant in reducing the number of financial statement restatements. The study recommended that the Kenya government should enact legislation that governs audit committees and impose stiff penalties on audit committees that are not effective.

All the studies reviewed indicate that the role of audit committees in corporate governance on financial performance is not clear. While Al-Baidhani and Al-Memun (2014) find that audit committees have a significant positive relationship with financial performance, Ojeka *et al.*, (2010) and Ogoro and Simiyu (2015) found that the different attributes of audit committee influence performance of firms differently. Specific studies relating to the relationship between audit committees and financial performance of KTDA factories in Kisii County are missing as indicated by the review.

2.3 Research Gap

The literature reviewed above has attempted to present the theoretical and empirical perspectives of the corporate governance strategy. On the basis of the respective studies which were reviewed, it was evident that there have been many studies examining the

relationship between corporate governance practices of board composition, stakeholder involvement and audit committees and performance. The role of stakeholder involvement on the financial performance of firms has not been established with certainty. This is because some studies find a significant positive relationship between stakeholder involvement and performance of firms while others found no significant relationship between stakeholder involvement and performance. Similarly, it is apparent that the role of board composition on financial performance has not been agreed upon by scholars with some finding no significant relationship between board composition and performance of firms and others finding that board composition does influence financial performance of firms positively and significantly so. Studies reviewed on the role of audit committees in corporate governance on financial performance have also elicited mixed results. Since this study will use board composition, stakeholder involvement and use of audit committees as proxies for corporate governance, and based on the reviewed studies, it is evident that the relationship between corporate governance practices and financial performance of KTDA factories has not been studied. This is the gap that this study will seek to fill.



CHAPTER THREE

RESEARCH METHODOLOGY

This chapter captures research design, target population, description of sample and sampling procedures, data collection procedures and instruments, validity and reliability of the research instruments as well as the data analysis procedures.

3.1 Research Design

This study employed a correlational research design. Sekaran (2004) defines a correlational research design as that design which not only attempts to establish a causal connection between one factor and another but also tries to establish the extent of the relationship. The correlational research will therefore provide quantitative data from the respondents that will be very important in answering the research hypothesis.

3.2 Study Area

This study was carried in Kisii County. The County is 350 kilometres west of Nairobi City on 0° 05' S, 37° 23' E and has a total of 7 tea factories with different locational characteristics. The factories serve approximately 92,000 farmers.

3.3 Target Population

The study targeted a population of 50 respondents that comprised of 28 directors and the 22 top managers drawn from different sections which included: the factory unit manager, production, field services and accounting. A pre-test of questionnaires was conducted on 5 directors and 5 top managers to test the valid and reliability of the data and a saturated sample of 23 directors and 17 top managers were conducted during the actual data collection exercise. These were considered to be the parties that are knowledgeable on governance issues which was important for the present study. The distribution of the population was as follows:

Table 3.1 Target Population

Factory	Directors	Top Managers
Ogembo	7	4
Nyamache	7	4
Itumbe	0	2
Kiamokama	7	4
Eberege	0	2
Rianyamwamu	0	2
Nyankoba	7	4
Total	28	22

Source: KTDA (2014)

3.4 Sampling Size

A saturated sample of 23 directors and 17 top managers was conducted after taking a total of 5 directors and 5 top managers for questionnaires pretesting. The census method was considered appropriate since the population of the study was small. Mugenda and Mugenda (2003) posit that where the population is less than 50, it is necessary to carry out a census of the population.

3.5 Data sources and Collection methods

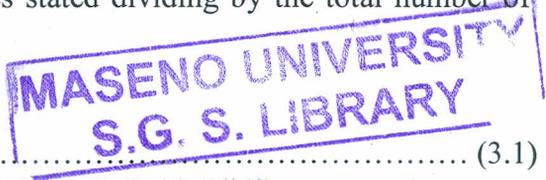
Both primary and secondary data were collected for this study. Primary data on corporate governance practices were collected using questionnaires while secondary data on financial performance were collected from records available at the factories.

3.6 Reliability Test and Validity Test

Reliability refers to the consistency of measurement (Mugenda and Mugenda, 2003). Reliability is increased by including similar items on a measure, by testing a diverse sample of individuals and by using uniform testing procedures. Reliability gives the internal consistency of data collected. This ensures that the data has certain internal consistent pattern. When no pattern is found in the responses, this indicates that probably the test is too difficult and as a result the respondents just guess the answers randomly. Reliability means that the findings would be consistently the same if the

study were done over again, (Creswell, 2009). In achieving this, test-retest coefficient was used to establish the reliability of the instrument. The data were collected from 5 directors and 5 top managers of the tea factories. The test-retest coefficient was found to be 0.83 as compared to a maximum of 1.0 indicating that the research questionnaire was reliable.

According to Mugenda and Mugenda (2003) validity is the quality attributed to proposition or measures to the degree to which they conform to establish knowledge or truth. An attitude scale is considered valid, to the degree to which its results conform to other measures of possession of the attitude. Validity therefore refers to the extent to which an instrument can measure what it ought to measure. It therefore refers to the extent to which an instrument asks the right questions in terms of accuracy. The researcher used Content Valid Index (CVI) which is a scale developed by computing or rating the relevant items in the instrument or questionnaire by checking their clarity, their meaningfulness in line with all objectives stated dividing by the total number of items. The validity was described as follows:



$$CVI = \frac{\text{Relevant items}}{\text{Total number of items}} \dots\dots\dots (3.1)$$

The CVI was found to be 0.79 indicating that the questionnaire was valid (Mugenda and Mugenda, 2003).

3.6 Data Analysis

Regression analysis was used to establish the relationship between the dependent and the independent variables. The following regression model was estimated.

$$\Pi_{ij} = \beta_0 + \beta_1 P_{1j} + \beta_2 P_{2j} + \beta_3 P_{3j} + e \dots\dots\dots (3.2)$$

Where:

Π_{ij} = Financial Performance (Profitability, ROA, ROI) of the i^{th} factory as perceived by j^{th} respondent.

β_0 = the constant term

β_1 = the coefficient of board composition in the relationship

β_2 = the coefficient for stakeholder involvement in the relationship

β_3 = the coefficient for Audit Committees in the relationship

e = is the error term which is assumed to be normally distributed with constant variance.

3.7 Data Presentation

The analysed data were presented in tables and charts.

Frequency

40

10

20

Source: Field survey (2017)

CHAPTER FOUR

RESULTS AND DISCUSSION

4.1 Response Rate

Questionnaire response rate is the proportion of the sample that participated in the survey as intended in all the research procedures. Out of 50 questionnaire forms administered to the top managers and Directors, of the 7 tea factories in Kisii County 40 were returned thus making a questionnaire response rate of 80%, indicating a high response rate. This is summarized in Table 4.1. The study aimed at collecting data with regard to the role of corporate governance practices on financial performance of KTDA factories. From the study, 40 questionnaire forms were answered and returned making a response rate of 80% while 10 questionnaire forms were not completely returned representing 20%. The Researcher considered that the response rate was significant enough to provide valid and reliable conclusions from the data collected towards satisfaction of the study objectives. According to Owens and Jonson (2003), a response rate of 80% is good enough to generate results for generalization

Table 4. 1 Response Rate

Questionnaire forms	Frequency	Percentage
Properly and fully answered.	40	80
Not returned	10	20
Total	50	100

Source: Field Survey (2015)

4.2 Background information on respondents

General information comprised data on the ranking of the respondents in terms of the capacity in which they serve, time served in the organization and the education level.

4.2.1 Rank of Respondents

The rank of the respondents was analyzed and tabulated in Table 4.2. The directors formed a larger percentage of respondents with a percentage of 55% while top management followed with a percentage of 45%. The bio data collected was useful in

providing more understanding about the target population. The average number of top management and directors respondents would mean that the information given is more objective to the study since most firms decisions are made by both the directors and members of the management. Additionally, from the above scenario, since most of the respondents were directors it can be concluded that directors are more involved in the management of factories than the top level management staff for they are elected by shareholders and represent their interests and understand more on the operations of the company than a top level management official. The management team has technical know-how and would be biased on matters that would lead to conflict of interest. Directors are more concerned with the financial well-being of the factory than any other officials within the factories hence their higher response rate.

Table 4. 2 Ranking of Respondents

Rank	Frequency	Cumulative frequency	Percentage
Top Management	18	18	45
Directors	22	40	55
Total	40		100

Source: field data 2015

4.2.2 Level of Experience in Management

The study sought to find out the period the respondents had served in management. The findings are shown in Table 4.3. The study established that all factories were governed with officials who had different time frame experience. From the findings in the table above, majority (68%) of the respondents had served for a period of between 5-10 years, 22% 2-5 years, 5% more than 10 years and 5% less than 2 years. These results had implications that majority of the management had enough experience to run the factories to achieve financial performance owing that majority had an experience of more than 5 years. But it can also be argued that no proper succession program has been put in place to ensure that young and inexperienced members of management are considered in taking over after retirement.

Table 4. 3 Level of Experience in Management

Period served	Frequency	Percentage %	Cumulative Percentage
Less than 2 years	2	5	5
2-5 years	09	22.5	27.5
5-10 years	27	67.5	95
More than 10 years	2	5	100
Total	40	100	

Source: field data 2015

4.2.3 Level of Education of Respondents

The study sought to find out the level of education of the respondents who gave their responses. The findings are shown in Table 4.4. The Table shows that majority (47.5%) of the management had an academic qualifications of certificate, 35% diploma, 12.5% masters and 5% bachelors. This indicates that the board membership was composed of members from different educational orientation and at least had some knowledge on management though the research indicated that a larger percentage of the board were below diploma. This could be a loophole for poor management in terms of decision making.

Table 4. 4 Level of Education of Respondents

Class	Frequency	Percentage %	Cumulative Percentage
Certificate	19	47.5	47.5
Diploma	14	35	82.5
bachelors	2	5	87.5
Masters	5	12.5	100
Total	40	100	

Source: field data 2015

4.3 Corporate Governance Practices

This study sought to establish the relationship between Stakeholder involvement, Board composition, Audit committee and financial performance. Correlation and regression analysis were employed in the study. Standard deviation measured the deviation of observed values from their mean. Table 4.5 shows the descriptive statistics for the study variables.

Table 4.5 Descriptive statistics for the study variables

	Stakeholder involvement	Board composition	Audit committee	Financial performance
N Valid	40	40	40	40
Missing	9	9	9	9
Mean	2.5650	2.1300	2.1150	1.7333
Median	2.9000	2.0000	2.0000	1.5000
Std. Deviation	1.08263	.84404	.86278	.86790
Skewness	-.065	-.036	-.042	1.366
Std. Error of Skewness	.374	.374	.374	.374
Kurtosis	-.879	-1.089	-1.191	1.388
Std. Error of Kurtosis	.733	.733	.733	.733
Minimum	1.00	1.00	1.00	1.00
Maximum	4.70	3.70	3.70	4.33

From Table 4.5 it can be inferred that the deviation of responses on extent of Stakeholder involvement, extent of Board composition, Audit committee and financial performance from their mean responses were 1.08263, 0.84404, 0.86278 and 0.86790 respectively. Since the deviations were more than the threshold of 0.5, it then implies that there were major deviations of the individual views from their mean responses. Skewness shows the extent to which a distribution differs from a normal distribution. A normal distribution normally revolves around zero. A positive skew means that the mean is greater than the mode while a negative skew means that the mean is less than the mode. The results show

that responses on Stakeholder involvement, extent of board composition, and audit committee were negatively skewed while financial performance was positively skewed. Although the values were positive in the case of independent variables, they suggest that the responses were normally distributed while responses on financial performance were not normally distributed as the value of the skew of the variables gravitated away from zero.

Standard error is a statistical term that measures the accuracy with which a sample represents a population. In statistics, samples mean deviates from the actual mean of a population; this deviation is the standard error. Table 4.5, the standard error of skewness is 0.374 meaning that the degree of sample skew disperses from that of the actual population by 37.4%. Kurtosis is a measure of the thickness or the thinness of the distribution's tail. It also measures normality of the distribution. As a rule of thumb, kurtosis for a normal distribution is 3. If it is greater than 3, then the distribution has a thick tail but if it is less than 3, the distribution has a thin tail. From Table 4.5, kurtosis for all the variables is less than three, thus the distributions had a thin tail, meaning the distributions were not normally distributed.

A correlation between the variables was also run. The findings of the correlation are shown in Table 4.6 below. Table 4.6 shows a strong positive significant association between stakeholder involvement ($r = .480, p = 0.002$), Board composition ($r = .511, p = .001$), audit committee ($r = .555, p = .000$) and financial performance. The association between board composition and audit committee is however very strong and significant ($r = .701, p = 0.000$). These results are in contradiction with those of Muchiri (2010) and Young (2001) who found no significant association between board composition and performance of firms. However, they are in agreement with studies by Al-Baidhani (2014) who found a significant association between existence of an audit committee and financial performance. This implies that firms which have instituted audit committees are more likely to perform better in terms of financial performance. The results also agree with those of Akodoh (2012), Miringu (2012), and Wu *et al.* (2013) who found a significant association between stakeholder involvement and performance of firms.

Table 4. 6 Correlation Matrix for the Study Variables

		Stakeholder involvement	Board composition	Audit committee	Financial performance
Stakeholder involvement	Pearson Correlation	1			
	Sig. (2-tailed)				
	N	40			
Board composition	Pearson Correlation	.267	1		
	Sig. (2-tailed)	.095			
	N	40	40		
Audit committee	Pearson Correlation	.199	.701**	1	
	Sig. (2-tailed)	.218	.000		
	N	40	40	40	
Financial performance	Pearson Correlation	.480**	.511**	.555**	1
	Sig. (2-tailed)	.002	.001	.000	
	N	40	40	40	40

** . Correlation is significant at the 0.01 level (2-tailed).

A multiple regression analysis was conducted. Results of the regression model are shown in Table 4.7 below.

Table 4. 7 Summary of the regression model on the effects of corporate governance practices on financial performance of KTDA factories.

R	Adjusted R Square	Std. Error of the Estimate	Change Statistics			Sig. F Change	Durbin-Watson	
			R Square	F Change	df1			df2
.679	.460	.66351	.460	10.243	3	36	.000	1.871

a. Predictors: (Constant), Audit committee, Stakeholder involvement, Board composition

b. Dependent Variable: Financial performance

Table 4.7, shows a coefficient of determination of 0.46, which means that 46% changes in financial performance of the tea factories is explained by the three independent factors of Audit committee, stakeholder involvement and board composition. This indicates a moderate significant influence of corporate governance practices on financial performance in line with previous studies such as those of Oketch (2004) and Kaptein (2003). Their studies showed that corporate governance practices generally have a significant influence on financial performance of firms. The value of Durbin-Watson was found to be 1.871, which is close to 2, an indication of the absence of auto-correlation. As a rule of thumb, a Durbin–Watson value of 2 suggests absence of autocorrelation (Odondo, Mukras and Momanyi, 2014).

To establish the effectiveness of the regression model, an analysis of variance was conducted. The results are shown in Table 4.8 below.

Table 4. 8 ANOVA results on the regression model

Model	Sum of Squares	df	Mean Square	F	Sig.
Regression	13.528	3	4.509	10.243	.000
Residual	15.849	36	.440		
Total	29.377	39			

a. Predictors: (Constant), Audit committee, Stakeholder involvement, Board composition

b. Dependent Variable: Financial performance

Table 4.8 shows an *f*-statistic (3, 36) of 10.243 which is significant at $p = 0.000$. This is a likely indication that audit committee, stakeholder involvement and board composition jointly explain a significant portion of financial performance of the tea factories. This revelation is in tandem with the significant coefficient of determination of 0.46 established in Table 4.7.

To establish the individual relationship between the independent variables and financial performance, a regression was run whose results are shown in Table 4.9.

Table 4. 9 Estimated coefficients of the independent variables

Model	Unstandardized Coefficients		Standardized Coefficients			Collinearity Statistics	
	B	Std. Error	Beta	T	Sig.	Tolerance	VIF
(Constant)	-.146	.357		-.409	.685		
Stakeholder involvement	.293	.102	.365	2.875	.007	.928	1.077
Board composition	.152	.180	.147	.844	.404	.491	2.037
Audit committee	.381	.173	.378	2.203	.034	.508	1.969

a. Dependent Variable: Financial performance

Table 4.9 shows that stakeholder involvement ($\beta = .293, p = .007$) and audit committee ($\beta = .381, p = .034$), both had significant positive effects on financial performance of the tea firms. This means that the more the stakeholders were involved in the decisions making process, the higher were the financial returns of the firms, and in this case, financial performance would significantly improve by 0.293. The involvement of audit committee in auditing done on a regular basis would also significantly improve performance by 0.381. Perhaps this was because the audit committees were effective in providing corporate governance that reduced the potential for fraudulent financial reporting as noted by Al-Mamun *et al* (2014). It also corroborates the results of Ojeka *et al* (2014) whose study in Nigeria focused on the effectiveness of audit committee on firm financial performance and found that certain measures of audit committee effectiveness such as audit committee independence, audit committee financial expertise and board size had positive coefficients and significantly influenced the firm's financial performance. Board composition on the other hand had insignificant positive effect on financial performance of the tea firms ($\beta = .152, p = 0.404$). The estimated variances of inflation factors (VIFs) are also less than 4, which suggest absence of serious multi-collinearity according to Pan and Jackson (2008).

CHAPTER FIVE

SUMMARY OF FINDINGS, CONCLUSIONS AND RECOMMENDATIONS

This chapter outlines summary of the findings, conclusions, recommendations, limitations and suggestions for further research to this study.

5.1 Summary of the Findings

The main objective of this study was to establish the relationship between corporate governance practices and financial performance of tea factories in Kisii County. The specific objectives were to; establish the relationship between the board composition and financial performance of KTDA factories in Kisii County; analyse the relationship between stakeholder involvement and financial performance of KTDA factories in Kisii County; and to assess the relationship between audit committees and financial performance of KTDA factories in Kisii County. The study revealed that corporate governance practices are moderately but significantly related to financial performance of the tea factories.

The first objective was to establish the relationship between the board composition and financial performance of KTDA factories in Kisii County. It was revealed that board composition has a positive but insignificant relationship with financial performance of the tea factories indicating that the way boards are composed in the tea factories does not have any influence on the financial performance of the factories.

The second objective was to analyse the relationship between stakeholder involvement and financial performance of KTDA factories in Kisii County. Results showed that stakeholder involvement has a positive and significant relationship with financial performance of the tea factories. This indicates that the more the involvement of stakeholders in decision making, the better the financial performance of the tea factories.

The third objective was to assess the relationship between audit committees and financial performance of KTDA factories in Kisii County. It was revealed that involvement of audit committee in auditing is positively and significantly related to financial performance of the tea factories implying that involvement of audit committees in

auditing done on a regular basis would significantly improve financial performance of the tea factories.

5.2 Conclusion

Based on the research findings, the following conclusions can be drawn. The first objective was to establish the relationship between the board composition and financial performance of KTDA factories in Kisii County. It was found that board composition has no significant relationship with financial performance of the tea factories and therefore concluded that this important corporate governance practice has not been understood well by the stakeholders since prior studies indicate that it significantly influences financial performance of firms.

The study findings based on the second objective indicate that stakeholder involvement has a positive and significant relationship with financial performance of the tea factories. It is concluded that the tea factories management have involved stakeholders in the running of the factories. However, since the financial performance of the factories is poor, it is concluded that the involvement of the stakeholders is not satisfactory.

Study findings based on the third objective indicate that involvement of audit committee in auditing is positively and significantly related to financial performance of the tea factories implying that involvement of audit committees in auditing done on a regular basis would significantly improve financial performance of the tea factories. The conclusion is therefore that involvement of audit committees is not done to the required levels since the factories are still performing poorly.

5.3 Recommendations

Based on the study findings and conclusions, the following recommendations can be made. Based on the finding that board composition has a positive but insignificant relationship with financial performance of the tea factories indicating that the way boards are composed in the tea factories does not have any significant influence on the financial performance of the factories, it is recommended that KTDA factories through the Agency actively restructure this corporate governance practice since prior studies reveal that it has a significant positive relationship with financial performance of firms.

Based on the findings from the second objective that stakeholder involvement has a positive and significant relationship with financial performance of the tea factories, it is recommended that this practice is enhanced to improve financial performance of the tea factories since the poor performance can be attributed to non-involvement of stakeholder.

Since the study revealed that involvement of audit committee in auditing is positively and significantly related to financial performance of the tea factories it is recommended that this corporate governance practice be enhanced by institutionalizing it in all the factories and enabling the committees so that they work more effectively.

5.4 Limitations of the Study

Even if this study makes significant contributions to the body of knowledge on effect of corporate governance practices on financial performance, it is imperative to evaluate the results in the context of its limitations. The first limitation is that the study focused only on the effect of corporate governance practices on financial performance of KTDA firms in Kisii County. This focus on a single sub-sector, region may make the results not generalizable to other manufacturing sectors.

Secondly, the study used questionnaires to capture important information pertaining to population with reference to study objectives. Although this practice is common in contingency based research, it has obvious disadvantages (Mugenda and Mugenda, 2003). Interview schedule should have been incorporated since some respondents were both illiterate and semi-illiterate respectively; therefore answering the questionnaire was a challenge. Personal interviews could have elicited greater information regarding participants' knowledge and attitudes. This method could have added important qualitative data and greater insight into the participants' thoughts and opinions.

5.5 Suggestions for Further Research

This study suggests that research be done on succession programs and their importance to financial performance. This study also suggests the need of training and development in improving financial performance.

REFERENCES

- Africa Development Bank (ADB) (2007), *Corporate Governance Strategy*, ADB.
- Akodo, R. (2012). Corporate governance and financial performance of public universities in Uganda. *Corporate Governance: An International Review*, 15(5), 935-43
- Al-Mamun, A., Yasser, Q., Rahman, A., Wickramasinghe, A., and Murugan, T. (2014) Relationship between audit committee characteristics, external auditors and economic value added of public listed firms in Malaysia. *Journal of corporate ownership and control*, 9(4).
- Blair, (1995), *Corporate governance and social responsibility*' [Online] available: <http://vig.prenhall.com/catalog/uploads/Wheelan-Hunger> Ch2. ppt, (26 2015).
- Braun, C. (2001). *Theories of Corporate Governance: the philosophical foundations of corporate governance*, Abingdon: Routledge.
- Committee on the Financial Aspects of Corporate Governance, (1992), *Report of the Committee on the Financial Aspects of Corporate Governance*, London: Gee.
- Davidson III, W N (2003): "Agency Costs, Ownership Structure and Corporate Governance Mechanisms", *Journal of Banking and Finance*, 27, 793-816
- Gani, L and Jermias, J (2006): "Investigating the Effect of Board Independence on Performance Across Different Strategies", *The International Journal of Accounting*, 41, 295-314
- Gay, L. (1992). *Educational Research: Competence for Analysis and Applications*. 4th Edition—New York: Macmillan Publishers.
- Creswell, J.C. (2009). *Research Design*. Sage Publishers, London.
- Hampel Committee, (1998). European Corporate Governance Institute. <http://www.ccg.or.ke>
- Hermes, F.G. (2004). *Strictly Board room: improving governance to enhance company performance*, (2nd ed.), Melbourne: Information Australia.
- Hendrik T, J. and Elaine R. (2009). *International Financial Statement Analysis*.

- Hutchinson, M (2002): “An Analysis of the Association between Firms’ Investment Opportunities, Board Composition, and Firm Performance”, *Asia Pacific Journal of Accounting and Economics*, 9, 17-39
- Jonathan M. (1994). Corporate Governance and Firm Performance.
- Kaptein, C. (2003). Boards, incentives and corporate social responsibility: the case for a change of emphasis, *Corporate Governance: An International Review*, 15(5), 935-43.
- Kenya Tea Development Agency (KTDA), (2013). Strategic Plan (2014-2018).
- Kiel, G. & Nicholson. (2003). *Boards That Work*, Sydney: McGraw-Hill.
- Kocmanova, A. and Simberova, I., (2012). Modelling Corporate Governance performance Indicators. Retrieved from the Internet, <http://doi.org> on 21st April, 2014
- Krejie, W.L. & Morgan, B. (1998). *Social Research Methods: Qualitative and Quantitative Approaches*, (6th Ed.), Boston: Allyn & Bacon.
- Krivogorsky, V (2006): “Ownership, Board Structure, and Performance in Continental Europe”, *The International Journal of Accounting*, 41, 176-197
- Maherm, P. & Zinkin, J. (1999). *Mastering Business in Asia Corporate Governance*. Asian Institute of Management, Philippine.
- Mallin, C.A. (2004). *Corporate Governance*, Oxford: Oxford University Press.
- Mensah, P. (2002). *Integrative Economic Ethics: Foundations of a Civilized Market Economy in Africa*, Cambridge: Cambridge University Press.
- Mensah, F., J. Blandin, N & O’Keefe, S. (2002). A new management model for government: integrating activity based cost in, the balanced scorecard and total quality management with the planning, programming and budgeting system, *International Public Management Review*, 5, 103–131.
- Meyer, J. (1996). *Corporate Governance and Accountability*, Chichester: Wiley.
- Miringu, G. (2013). Corporate governance in Schools in Central Kenya, *Corporate Governance*, 1(4), 4-8.

- Muchiri, K.(2010). Corporate governance – the global state of the art, *Corporate Governance: An International Review*, 7(2), 117-122.
- Murthy, N. R. (2003). Report of the SEBI Committee on Corporate Governance.
- Mugenda, O and Mugenda, A (2003). *Research Method, Quantitative and Qualitative Approaches*. Nairobi: ACTS.
- Mulili, B. M & Wong, P (2011). Corporate Governance Practices in Developing Countries: The Case of Kenya. *International Journal of Business Administration*, 2(1).
- Odondo A. J; Mukras, M. S. and Momanyi, G. (2014). Determinants of Sweet Potatoes (*Ipomoea batatas* L) Profitability in Rachuonyo South District, Kenya. *International Journal of Managerial Studies and Research (IJMSR)*, 2 (4): 48-60
- Ogoro. G.O and Simiyu. C. N (2015). Effectiveness of Audit committee in the public sector: A case of Parastatals in Kenya. *Journal of Finance and Accounting*, 6 (4): 56-65.
- Ojeka, S., Iyoha, F., Odianonsen, F., and Foyeke, I.K., (2014), Effectiveness of Audit Committee and Firm Financial Performance in Nigeria: An Empirical Analysis, *Journal of Accounting and Auditing: Research & Practice*, 2014(1)
- Oketch, M. (2004). UNDP on good governance, *International Journal of Social Economics*, 29(1), 108-120.
- Opondo, M (2009). Corporate governance in the Agricultural industry in Kenya. *Journal of Corporate Governance*, 52(1), 18- 25.
- Organization for Economic Cooperation and Development, (2011), *Corporate Governance: improving competitiveness and access to capital in global markets*, a report to the OECD by the Business Sector Advisory Group on Corporate Governance, Paris.
- Owens, L. & Jonson, T. P (2003), "Survey Response Rate Reporting in the Professional Literature." Paper presented at the annual meeting of the American Association for Public Opinion Research, Sheraton Music City, Nashville, TN. Retrieved from http://www.allacademic.com/meta/p116171_index.html
- Pan, Y, and Jackson, R. T. (2008): Ethnic difference in the relationship between acute Inflammation and serum ferritin in US adult males. *Epidemiology and Infection*, 136, 421- 431.

- Private Sector Initiative for Corporate Governance, (2012). *Principles for Corporate Governance in Kenya*. Private Sector Corporate Governance Trust, Nairobi.
- Rabelo, S., (2002). *A New Way to Govern Organization and Society after Enron*, London: New Economics Foundation.
- Ramon, V.R. (2001). Corporate Governance as Competitive Advantage in Asia: Managing Corporate Governance in Asia, *Asian Institute of Management*, Philippines.
- Reed, J.E. (2001). *Essentials of Corporate Management in Asia*, *Journal of Finance*, 52(2), 737-783.
- Rogerson, P. A. 2001. Statistical methods for geography. London: Sage Publications.
Retrieved from <http://www.amazon.com/exec/obidos/ASIN/0761962875/#reader>
- Rwegasira, K., (2000). Corporate governance in emerging capital markets: will it work in Africa? *Corporate Governance: An International Review*, 8(3), 258-67.
- Salacuse R.W. (2009). A survey of corporate governance, *The Journal of Finance*, 2(2), 77-83.
- Spong, K and Richard J. (2007). Corporate Governance and Bank Performance, Federal Reserve Bank of Kansas City.
- Tsameny, S.(2007). Corporate governance: Its scope, concerns & theories, *Corporate Governance: An International Review*, 5(4), 180-205.
- Wanyande, P. (2009). *Problems ailing the tea industry in Kenya*. A report by the Transparency International. Nairobi.
- Wu, G. (2000). Governance and moral failings in Asia, *Corporate Governance*, 2(2).
- Yoga B, O. (2006): *Corporate Governance and Firm Performance of Financial Institutions Listed in Nairobi Stock Exchange*, published MBA- project University of Nairobi, Kenya