Influence of Corporate Governance Structure on Financial Performance: A Case of Listed Commercial Banks in Kenya

Benedicta K. Kamazima, Paul Mathenge and Thomas Ngui

Abstract
This study aimed at establishing the effects of corporate governance practices and policies on the financial performance of listed commercial banks. A cross-sectional research design was used in the study. Whereas there has been renewed interest in corporate governance, there is a paucity of relevant data from empirical studies. The study sought to eliminate the limitations in the depth of the understanding of corporate governance issues with respect to financial performance in the banking sector. The population involved were all the 10 listed commercial banks in Kenya. Return on assets and return on equity were key variables that defined bank performance; whereas firm size was adopted as a control variable. Corporate governance structures were measured using board of directors, ownership structure, and audit committee structure. The study used secondary data which was gathered from company annual financial reports, company websites and other financial statements spanning a period of five years from 2012-2016. Data analysis was primarily done using descriptive and inferential statistics. Under descriptive statistics; mean, maximum, minimum and standard deviation were used and under inferential statistics; Pearson correlation analysis and multiple regression analysis were employed. The findings of the study among others indicated that there is a negative and significant relationship between Board of Directors, ownership structure and audit committee structure with the financial performance of listed commercial banks in Kenya in terms of Return on Assets (ROA) and Return on Equity (ROE). Specifically, the study concluded that the number of board committees, number of non-executive directors, percentage of foreign ownership and number of audit committee meetings have a positive impact on the financial performance of commercial banks while board size, government ownership, and board diversity have a negative impact on financial performance of listed commercial banks.

Keywords: corporate governance, firm financial performance, return on assets, return on equity, Nairobi Stock Exchange, Kenya.
Corporate governance is defined as “the system by which companies are directed and controlled” (Cadbury, 2012). In the banking industry, corporate governance involves the way banking institutions’ business and affairs are managed by the board of administration and the top management, which affects how the bank works to meet its objectives, plans and policies, day to day work management, protection of the rights and interests of stakeholders, commitment to sound and safe professional behaviors and practices (Linyirue, 2006). In Kenya, corporate governance is indeed gaining some level of recognition, though limited even in the well-regulated institutions and sectors. The Kenya Capital Market Authority has issued guidelines on corporate governance practices by the public companies in Kenya. The guidelines were developed in recognition on the role of good governance in corporate performance, capital formation and maximization of shareholders values and protection of investors’ rights (Wamalwa, 2013). The main objectives of these rules are to strengthen corporate governance practices in public listed companies in Kenya and to bring the level of governance in line with international standards. Corporate governance has become one of the most discussed topics in business administration due to balance sheet manipulation or even collapse of some public corporations. Despite this urgency, empirical research on this phenomenon is still in its infancy in the East African region and in Kenya in particular. The study, therefore, intended to contribute to the filling of this gap.

Financial Performance
Performance is defined as the reflection of the way in which the resources of a company are used in the form which enables it to achieve its objectives (Heremans, 2007). According to Werther and Chandler (2010), financial performance is the process of measuring the results of a firm’s policies and operations in monetary terms. It is used as a measure of the organization’s financial health. Furthermore, it can be used to make comparisons between firms in the same industry or compare various industries or sectors in aggregation.

Commercial Banks in Kenya
In Kenya, there are a total of 44 commercial banks with two banks – Chase Bank and Imperial Bank in receivership. The commercial banks dominate the financial sector (Ongore & Kusa, 2013) in the country. It is known that in a country where the commercial banks lead the financial sector, failure in the sector has an enormous implication on the economic growth of the country. In this regard, the banking sector in Kenya has experienced numerous regulatory and financial reforms that have brought valuable changes to the banking sector. The banking sector is heavily regulated by the Banking Act under the Central Bank of Kenya (CBK) regulations. Among other regulations, all commercial banks operating in Kenya are obligated to submit annual audited reports to the Central Bank.

Statement of the Problem
The ultimate objective of corporate governance is to achieve the highest degree of harmony within the organizational structure. However, recent studies have shown that many organizations have side-lined the significance of corporate governance as a mechanism for the attainment of organizational strategic goals. Past empirical studies examining the relationship between governance and financial performance produce mixed results. While some studies have shown no significant relationship between governance and financial performance, others have shown a positive relationship between corporate governance and financial performance. In Kenya, studies conducted in the financial services sector have focused mainly on other financial sectors rather than commercial banks, despite the fact that banking industry is an important player in Kenya’s economy. There are, therefore, limitations
in the depth of understanding of corporate governance issues with respect to financial performance in the banking sector. Whereas there has been renewed interest in Corporate Governance, there is a paucity of relevant data from empirical studies. The previous studies were carried out several years ago. Hence, the current study needed to bring in the dynamics that have developed in the corporate governance and financial performance. This study sought to bridge these huge gaps by investigating the influence of Corporate Governance on the financial performance of listed commercial banks in Kenya using the 2012-2016 data to provide more empirical data in the study area.

Research Objectives
The main objective of the study was to evaluate the influence of corporate governance structure on the financial performance of listed commercial banks in Kenya. The study was guided by the following specific objectives:

1. To examine the influence of board of directors on the financial performance of listed commercial banks in Kenya.
2. To explore the influence of ownership structure on the financial performance of listed commercial banks in Kenya.
3. To establish the influence of audit committee structure on the financial performance of listed commercial banks in Kenya.

Research Questions
The study was guided by the following research questions

1. What is the influence of the board of directors on the financial performance of listed commercial banks in Kenya?
2. What influence does the ownership structure have on the financial performance of listed commercial banks in Kenya?
3. What influence does the audit committee structure have on the financial performance of listed commercial banks in Kenya?

Literature Review
A corporate governance system that is transparent and functional has the ability to appeal to investors and enhance the foundation for financial performance (Marx, Van der Watt, Bourne, & Hamel, 2004). Despite the crucial role that corporate governance plays in driving the performance of the firm, there is still a gap in the level of understanding on this critical subject. This is due to the scarcity of literature on corporate governance specifically in the emerging economies such as Kenya, caused by immature business sectors and weak regulatory frameworks among others. Previous studies on the influence of corporate governance on firm performance have inconsistencies in which some studies concluded that there was a positive association, others concluded that there was a negative association, while other scholars found no association between the two variables. With regard to these incongruities the research aimed at determining the influence of corporate governance structure on firm financial performance using ROE and ROA as the dependent variables measuring financial performance.

Theoretical Framework
Agency Theory
Companies that are listed on the stock exchange have organizational frameworks in which ownership and control between principals and agents are fundamentally separated. In this
relationship, the principals hire agents to manage the entity in view of their interests while paying the agents for the work done (Jensen & Meckling, 1976). Conflicts of interests are the central base of the agency theory which disrupts the principal-agent relationship caused by the disparity of the interests of the managers and shareholders. In this instance, the agents (managers) are thought to be rational but opportunistic. This potential relationship problem between principals and agents has been conceptualized by the agency theory (Fama & Jensen, 1983). Conclusively, the theory is primarily concerned with ownership structures and organizational structures that influence agency conflicts.

**Resource Dependence Theory**

Pursuant to the dependence theory, frameworks of corporate governance including the board of directors influence the entity’s access to resources that facilitate the entity’s performance (Pfeffer, 1973). The theory specifically supports boards having a large number of non-executive directors so as to bring in their wide knowledge and experience that will heighten the reputation of the entity (Haniffa & Hudaib, 2006). Conclusively, this theory utilizes boards’ external connections and relationships to improve the entity’s performance (Muth & Donaldson, 1998; Nicholson & Kiel, 2007).

**Stewardship Theory**

In consonance with the Stewardship Theory, the members of the entity possess some kind of positive common character that spawns trustworthy behaviour (Davis, Schoorman & Donaldson, 1997). The theory continues to assert that agents are always concerned with their own fame and career advancement which in turn restricts them from acting contrary to shareholders interests, leading to minimized costs (Donaldson & Davis, 1994).

Contrary to the Resource Dependence Theory, the Stewardship theory favours a board that is widely dominated by members from within the entity because the members are well conversant with the entity’s operations including technical knowledge and expertise (Muth & Donaldson, 1998). The state of the Chairperson being the CEO of the entity simplifies leadership and control and facilitates consistency especially in decision making, which is thought to add up to the superlative effectiveness of the entity (Donaldson & Davis, 1991).

**Corporate Governance Structure and Financial Performance**

**Board of Directors and Financial performance**

The fundamental role of the board of directors is to monitor the managerial side of the firm and to minimize the problems inherent in the principal-agent relationship. In this sense, principals are the owners, agents are the managers and the board of directors acts as the monitoring mechanism. In situations when the interests of the agent and the principal are misaligned, an agency problem exists, which in the short or long term adversely affects the overall organizational performance (Mallin, 2002).

According to Lim (2010), the board is the most fundamental corporate governance structure in any organization. To enhance monitoring and ensure that resources are allocated and applied to the intended purpose, shareholders choose among themselves individuals to represent them on the boards. This structure is put in place to safeguard the interests of the owners of resources who are the principals thus an attribute to organizational performance. Boards are meant to ensure that the self-seeking venture that management may have are limited or curtailed (Ahmed & Wang, 2012). Essentially, boards are the link between the investors and management since they ensure capital and other resources are directed to the right purpose to enhance performance (Brown, 2007).
The relationship between the board composition and its impact on performance is extremely questionable. The directors can be categorised as executives, taking the roles of managers, or non-executive directors. Each group is differentiated from another by having its own incentives and behaviours (De Andres, Azofra, & Lopez, 2005). However, most national and international corporate governance codes support the blend of these two categories, for example, the Sarbanes-Oxley Act in the U.S and the OECD code.

According to Maher and Anderson (1999), in systems characterized by weak owners, boards, like management, can easily become entrenched. Therefore, board composition may influence strategic decision-making and subsequently firm performance (Letting, Nicholas, Aosa, & Machuki, 2012). Good corporate governance keeps the organization in business and guarantees an organization's future success. A well composed and established board is important for organizational performance. It further ensures proper utilization of resources available.

The right board size is another issue on an unending debate on corporate governance structures. Some argue for small boards while others insist on large boards. According to Hermalin and Weisbach (2001), large boards consume a lot of time in the decision-making process because it is difficult to arrive at a consensus and they lack cohesiveness. Thus, the problem of coordination outweighs the advantages of having more board members. When boards consist of too many members, agency problems may increase because some board members may tag along as free riders thus hampering organizational performance (Haniffa & Hudaib, 2006). Conversely, according to Dalton and Dalton (2005), small boards may lack the advantage of having the spread of expertise, experience, and representation.

According to Adams, Hermalin, and Weisbach (2005), large boards are prone to encounter high costs in monitoring the organization and at the same time they seem to be ineffective when board members are more than seven or eight people. Additionally, the agency model proposes that as the size of the board increases, the organization’s problem regarding director free riding escalates, thus the board becomes less significant and minimally involved in the management process (Hermalin & Weisbach, 1998). On the other hand, other researchers assert that as the size of the board increases, the performance of the organizations likewise increases. As Laimon and Vafeas (2010) blatantly stipulated in their study that the market responds positively when the board size increases, large boards monitor organizational performance better because of their diverse background and skills.

The number of board meetings is an unending discussion on corporate governance structures. Vefeas (1999) explains that an important proxy for measuring the intensity and effectiveness of corporate governance monitoring and disciplining is the frequency of board meetings. It has been contended that a higher frequency of board meetings may result in a higher quality of managerial monitoring and therefore impacts positively on corporate performance. Regular meetings can help directors to remain more informed and knowledgeable about important developments within the firm and thereby place them in a better position to timely address emerging critical problems (Mangena & Tauringana, 2007). Ntim and Oseit (2011) conducted a study in South Africa on the frequency of board meetings and corporate performance. Their findings suggested that boards that meet more frequently tend to generate higher financial performance.
On the other hand, other researchers do not consider board meetings necessarily valuable. Vafeas (1999) argues that board meetings are not useful due to the limited time non-executives spend with the company and such time could be better utilised for a more meaningful exchange of ideas with the management. Similarly, regular meetings involve managerial time and increase travel expenses, administrative support requirements and directors’ meeting fees. This may affect enterprise activities within the firm as resources are being channelled towards less productive activities (Evans, Evans, & Loh, 2002).

The number of board committees is another corporate governance issue of major importance. To effectively monitor executive management and perform other tasks involving serious agency problems, such as setting executive remuneration, engaging external auditors, and hiring and firing CEO, boards are often subdivided into smaller committees (McClogan, 2001). Board committees provide a means and structure for effective governance by facilitating special tasks and addressing important corporate concerns (Bilimoria & Piderit, 1994). Typically, there are three main board committees that support the work of the board; this includes the audit, remuneration, and nominations committee (Anand, 2007). Conceptually, these standing committees assist the board to perform its oversight responsibilities. The committees are composed of expertise board members who technically deal with specialized issues that the board as a whole will waste much time in handling.

The association between board structure and firm performance has been heavily discussed, but few studies have focused on the role of committees. Board committee literature in many instances has examined the effect of single board committees rather than the entire standing committees of the board (Newman & Mozes, 1999; Sun & Cahan, 2009) making it difficult to link board effectiveness to board standing committees. Against this backdrop, this paper provides an examination of how the number of board committees influences the financial performance among listed commercial banks in Kenya.

Board diversity has been a growing area of corporate governance research in recent years (Habbash, 2010). According to Carter, Simkins, and Simpson (2003) gender remains one of the most significant governance issues faced by managers, directors, and shareholders of the modern business world. One of the central propositions of the business case for board diversity is that women and minority directors provide significant unique information to the board and managers which improve strategic decision making (Burke, 2003).

Ownership Structure and Financial performance
According to Ongore (2011), the board alone cannot be a panacea to all governance problems. He argues that research on ideal corporate governance structures pays inordinate attention to the role of the Board to the exclusion of other equally important aspects of governance such as ownership structure. The risk-taking orientations of their shareholders as these have a direct bearing on the type of investment decisions that managers will prefer (Shleifer & Vishny, 1994). Different ownership structures manifest themselves in the governance of organizations differently. These could include foreign and government ownership.

Foreign investments are the centre of economic development; they occupy a special place in most countries seeking to draw more capital through financial liberalization, privatization, and IPO (Moez, Marouan, & Tahar, 2015). Recent literature is beginning to show the link between the role of foreign ownership in corporate governance and firm performance. It is duly accepted that foreign ownership plays a crucial role in firm performance, particularly in developing and transitional economies. Researchers such as Aydin, Sayim, and Yalama (2007) have concluded that, on average, multi-national enterprises have performed better than
the domestically owned firms. It is claimed that firms benefit from a high level of foreign ownership because foreign investors demand higher standards of corporate governance. If foreign investors assume a role of active monitors, firm performance is expected to increase as foreign ownership increases.

Following the agency theory foreign ownership is expected to put together shareholders’ interests with agents and in so doing reduce the problem of the agents while maximizing the wealth of shareholders, thus leading to terrific organization performance. Basing on that, this study looked at how foreign ownership of banks in Kenya influenced the performance of listed commercial banks financially.

On banks government ownership, Porta, Lopez-de-Silanes, Shleifer, and Vishny (1999) affirm that the government enticement to take shares in an entity can be associated with political intentions. However, the government can take a big chunk of equity in an entity so as to exercise power on the entity. This can take place due to the fact that most managers have a habit of trying to achieve their own self-interests. In addition, the government including politicians and bureaucrats incline to use entity’s assets in order to attain their objectives. That is to say, governments are mostly interested in governing ownership rights and not flow rights, a situation that affects the performance of the entity.

Likewise, Najid and Rahman (2011) assert that entities owned by the government are not innovative and lack entrepreneurial skills. They are also politically motivated instead of commercially motivated, thus leading the entity to perform poorly in finance. Furthermore, Mak and Li (2001) contend that government-owned entities experience poor monitoring and accountability, the facts that put them in a situation of failing to embrace good governance mechanisms.

Audit Committee and Financial Performance

An audit committee is an important corporate governance mechanism in firms to protect the interests of shareholders and oversee financial reporting (Mallin, 2002). According to the agency theory, there is a positive and significant association between the presence of an audit committee and the quality of financial statements (Felo, Krishnamurthy, & Solieri, 2003). In addition, the audit committee can be effective in protecting the interests of shareholders and ensuring the reliability of information that is disclosed. The responsibility of an audit committee is to oversee the transparency of financial reports and ensure the objectivity of an external audit by providing a channel of communication (Vicknair, Hickman, & Carnes, 1993).

In regard to the size of an audit committee, De Angelo (1981) argued that large audit committees can contain the loss of a client and, therefore, will provide a higher quality of the audit. In support, Davidson (1993) used an indirect method to indicate that size is a good proxy for a quality structured audit committee. He argued that managers have incentives to manipulate the reported earnings to meet the analyst’s forecasts. Therefore, if large auditing firms provide higher-quality audits than small auditing firms, it may be expected that the forecast errors of big auditing firms’ clients will be larger than those of small auditing firms’ clients. Bouaziz (2012) showed that auditor size has an important impact on the financial performance of firms in terms of return on assets and return on equity.

To pursue their various functions, the audit committee must meet regularly with the external and internal auditors to review the financial statements, audit process and internal controls of the firm. Audit committee meetings refer to the frequency by which the committee meets together. The average number of audit committee meetings refers to the level of audit
committee activity (Xie, Davidson, & DaDalt, 2003; Menon & Williams, 1994). Al-Mamun, Yasser, Rahman, Wickramasinghe, and Nathan (2014) views that regular meetings of audit committee could help reduce agency problems and information asymmetry of a firm by providing fair and timely information to investors. DeZoort, Hermanson, Archambeault, and Reed (2002) proposed that a company where the audit committee met more frequently was likely to be more careful in safeguarding the interest of its investors. Morrissey (2000) suggests four meetings in a year for audit committees. He further observes that best quality of financial reports can be assured if four sittings are held during the year.

**Empirical Review**

Dzingai and Fakoya (2017) examined the influence of corporate governance structures on firm financial performance in South Africa among selected mining companies listed on the Johannesburg Stock Exchange (JSE). Secondary data was collected from 2010-2015 and was analysed using two-panel data techniques; the fixed effects model and the random effects model. Corporate governance variables were board size and board independence while the financial performance was measured by return on equity (ROE). Firm size and sales growth were used as control variables. The results suggested that a small board is likely to lead to a higher performance because it avoids the problem of free riding which occurs among large boards. The study also found a positive relationship between board independence and the firm performance as measured by ROE implying that the more independent non-executive directors are on the board, the more profitable the firm is likely to become.

Zábojníková (2016) conducted a study on the impact of audit committee characteristics on firm financial performance in the UK. The four main audit committee attributes explored were audit committee size, the frequency of its meetings, the number of independent directors and the financial expertise of its members. The firm financial performance was measured by return on equity (ROE) and Tobin’s Q. The control variables used in the study were the firm size and firm leverage. The study used a sample of 72 British non-financial UK companies listed on the London Stock Exchange. The fixed effect panel data regression model was used to analyse panel data for examining the association of audit committee characteristics with the financial performance of firms. The main findings of the study suggested that the features of audit committees have an impact on UK firm performance. Specifically, the findings suggested that there is a significant positive relationship between the audit committee size, frequency of its meetings and its financial experience and firm financial performance. On the contrary, the audit committee independence appeared to be negatively correlated with firm performance.

Puni (2015) examined the effect of board committees on corporate financial performance among companies listed on the Ghana Stock Exchange (GSE). The quantitative research approach was adopted to study the prognostic effect of the board committee on corporate financial performance for companies consistently listed on the GSE from 2006-2010. Data was sourced from annual reports of listed companies and a static panel regression model was employed to analyse the presence of various committees on corporate financial performance. The results indicated that board committees had no statistically significant effect on the corporate financial performance of listed firms. The outcome suggests that the internal workings of corporate boards were weak implying that the effective supervision expected of these committees in terms of executive recruitment, succession planning, internal control, effective financial reporting, and the fixation of executive remuneration is lacking. The author recommended that board committees be strengthened with capable outside directors, skilful in the various technical areas to assist committees to deliver on their responsibilities by instituting transparent selection processes.
Choe and Lee (2015) carried out a study on the effect of ownership structure on banks’ performance in South Korea. The authors collected time series data for the period of 1998 – 2002. The study employed the simple ordinary least square model to carry out data analysis. The study reported that the existence of one foreign ownership director improves bank performance significantly, but multiple foreign directors in the organization do not improve bank performance. They, therefore, concluded that in order for commercial to enhance financial performance, they should minimize the number of foreign directors who act as the representative of the firm owners’ interest at the bank.

Bennedsen, Kongsted, and Nielsen (2014) conducted a study on the effect of board size and board independence on the performance of small and medium-sized corporations in Denmark. The primary data was collected from 111 SMEs by means of questionnaires. The study then used both simple and multiple regression methods to carry out data analysis. The study found that board size has no effect on performance for a board size of below six members, but found a significant negative relation between board size and performance when the board size increases to seven or more members whereas board independence had significant positive relation to performance. The study concluded that board size and board independence have effects on the performance of Danish SMEs.

Most research administered regarding corporate governance and bank performances have focused on one corporate governance aspect that affects the banking sector performance. In Kenya, studies conducted in the financial services sector have focused mainly on other financial sectors rather than commercial banks, despite the role the banking industry plays in Kenya’s economy. Thus this research integrated various corporate governance variables (board of directors, audit committee, and ownership structure) to determine their overall influence on the financial performance of the listed commercial banks in Kenya.

Methodology
The research made use of secondary data collected from company annual financial reports, company websites and other financial statements covering a period of five years from 2012-2016.

Research Design
The research study employed a cross-sectional research design. A cross-sectional design refers to any collection of data from a sample of individuals (or groups) at a particular point in time as a basis for inferring the characteristics of the population from which the sample covers (Creswell, 2009). This is mainly because the focus of the research was to gain an understanding and insight on the role of corporate governance on the financial performance of listed commercial banks in Kenya using the quantitative data which was collected. The research was interested in the state of affairs already existing and no variable was manipulated. This design is supported by Adekunle and Aghedo (2014) who also adopted a cross-sectional research design to analyse the relationship between performance and corporate governance systems of some quoted companies on the Nigerian Stock Exchange.

Area of the Study
The study was conducted in the capital city of Nairobi in Kenya. Kenya is located in Eastern Africa bordering the Indian Ocean, between Somalia and Tanzania. The author felt that it was important for the study to be conducted in this city because Nairobi is the economic hub of
East Africa and is home to the head offices of all the commercial banks listed on the Nairobi Stock Exchange.

Kenya has a population of approximately 49.7 million (United Nations, 2017) distributed into more than 40 different ethnic groups. The Kikuyu is the largest group constituting about 12 percent of the population. The official languages spoken in Kenya include Swahili and English. Swahili is essentially a Bantu language though deeply influenced by Arabic. With regards to religion, Kenya has no official religion. However, Christians make up more than 50 percent of the population.

Population of the Study

Method of Data Collection and Analysis
The study utilized secondary data gathered from company annual financial reports, company websites and other financial statements spanning a period of five years from 2012-2016. Since the study aimed at investigating the influence of corporate governance structure on the financial performance of listed commercial banks in Kenya, the study employed Pearson correlation and multiple regression analysis. Statistical Package for Social Scientists (SPSS) version 21 was used to run the analysis of the data.

Research Findings
The following section presents findings and discussion of results in relation to how corporate governance structure influences financial performance of listed commercial banks in Kenya. Data was collected using secondary sources (that is, annual financial reports) from 10 commercial banks listed by the Central Bank of Kenya.

Descriptive Statistics
Trochim (2006) contends that, along with simple graphics analysis, descriptive statistics virtually forms the basis of every quantitative analysis of data. In this study, descriptive statistics were employed to provide: means, maximum, minimum and standard deviation of data collected on corporate governance and performance of the listed commercial banks in Kenya.
As shown in the table above, the findings indicate that listed commercial banks in Kenya had an average board size of 10 members, with the highest bank having a maximum board size of 12 members while the lowest bank had a minimum board size of 8 members. The study also revealed that the banks had an average of 2 executive directors and 8 non-executive directors. The findings further indicated that listed commercial banks in Kenya held an average of 7 board meetings in a year with the highest bank held 14 board meetings while the lowest bank held 4 meetings in a year. The findings showed that government ownership of the banks was 4.07 percent while foreign ownership stood at 30.8% among the listed commercial banks. Financial performance of commercial banks was measured using Return on assets (ROA) and Return on Equity (ROE). The findings indicate that the listed commercial banks in Kenya reported an average return on asset of 2.9292% with the maximum of 4.74% and minimum of -0.009% that deviated by 1.29% on both sides of the mean. This implies that the standard deviation was relatively low. When return on equity (ROE) was employed as a performance measure, the findings indicate that commercial banks in Kenya reported an average return on equity of 17.972% with a maximum of 29.075% and a minimum of 1.341% that deviated by 7.422% on both sides of the mean. The standard deviation of 7.422% indicated a relatively high disparity in ROE.
### Pearson Correlation Analysis

<table>
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<tr>
<th>control variables</th>
<th>Board size</th>
<th>No. of board meetings</th>
<th>No. of board committees</th>
<th>No. of executive directors</th>
<th>No. of non-executive directors</th>
<th>% of government ownership</th>
<th>% of foreign ownership</th>
<th>Audit committee size</th>
<th>No. of audit committee meetings</th>
<th>Return on Assets (ROA)</th>
<th>Return on Equity (ROE)</th>
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<td>-.132</td>
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<td>-.543</td>
<td>-.431</td>
<td>.211</td>
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<td>No. of board meetings</td>
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<td>.</td>
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<td>.367</td>
<td>.294</td>
<td>.002</td>
<td>.231</td>
<td>.224</td>
<td>.065</td>
<td>.124</td>
<td>.293</td>
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<td>No. of board committees</td>
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<td>.284</td>
<td>-.084</td>
<td>-.492</td>
<td>.750</td>
<td>-.129</td>
<td>.152</td>
<td>.652</td>
<td>-.073</td>
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<tr>
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<td>.229</td>
<td>.415</td>
<td>.089</td>
<td>.010</td>
<td>.371</td>
<td>.348</td>
<td>.028</td>
<td>.426</td>
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<td>.469</td>
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<td>No. of non-executive directors</td>
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<td>.549</td>
<td>-.348</td>
<td>.501</td>
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<td>-.150</td>
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<td>.440</td>
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<td>.179</td>
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<td>.423</td>
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<td>.260</td>
<td>.316</td>
<td>.477</td>
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</tbody>
</table>

The study findings presented show that the correlation between ROA with each of the variables of corporate governance namely: Board size, number of board meetings, number of board committees, number of executive directors, number of non-executive directors, percentage of government ownership, percentage of foreign ownership, audit committee size and number of audit committee meetings was not statistically significant at 5% level (p.value 0.293, p.value 0.426, p. value 0.351, p. value 0.016, p. value 0.313, p.value 0.477, p.value 0.109, p.value 0.035 and p. value of 0.323 respectively). In other words, this means that correlations between the independent and ROA do not exist above and beyond the effects of bank size. Invariably meaning that the above corporate governance mechanisms have got no effect on the ROA of listed commercial banks in Kenya after controlling for the effect of bank size.

Similarly, the study established that there was a negative and insignificant correlation between Return on Equity and Board size, number of board meetings, number of board committees, number of executive directors, number of non-executive directors, the percentage of government ownership, the percentage of foreign ownership, audit committee size and number of audit committee meetings. However, these variables were found to be significantly correlated with ROE at 5% level (p.value 0.293, p.value 0.426, p. value 0.351, p. value 0.016, p. value 0.313, p.value 0.477, p.value 0.109, p.value 0.035 and p. value of 0.323 respectively). Hence, the conclusion is that these corporate governance mechanisms have a statistically significant impact on ROE above and beyond the effects of bank size.
size and number of audit committee meetings. The p.value of the independent variables included: 0.071, 0.335, 0.469, 0.359, 0.124, 0.299, 0.445, 0.222 and 0.045 respectively. This means that all the p.values were above 0.05 thereby implying that the correlation between independent variables and ROE does not exist above and beyond the effect of bank size.

Multiple Regression Analysis

ROA as a dependent variable

A multiple regression model utilized the relevant available data on the dependent and independent variables from 10 commercial banks listed by the central bank of Kenya. The dependent variable (financial performance) was measured using the financial ratio of return on assets (ROA) and the independent variables relating to Board size, number of board meetings, number of board committees, number of executive directors, number of non-executive directors, percentage of government ownership, percentage of foreign ownership, audit committee size and number of audit committee meetings.

The multiple linear regression model structure can be summed up as:

$$ FP = \beta_0 + b_1BOD_{1t} + b_2OWNS_{2t} + b_3ACS_{3t} + e_i $$

Where

- $FP = ROA$
- $\beta_0 = $ Regression constant to be estimated
- $\beta_1$ to $\beta_4 = $ Regression coefficients to be estimated
- $BOD_{1t} =$ Board of Directors (Board size, board meetings, number of board committees, number of executive and non-executive directors and board diversity)
- $OWNS_{2t} =$ Ownership Structure (percentage government ownership and foreign ownership)
- $ACS_{3t} =$ Audit Committee structure (audit committee size and number of audit committee meetings)
- $e =$ Error /Disturbance Term

Table 2: Regression Analysis Output

<table>
<thead>
<tr>
<th>Model</th>
<th>R</th>
<th>R Square</th>
<th>Adjusted R Square</th>
<th>Std. Error of the Estimate</th>
<th>Change Statistics</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>.900&lt;sup&gt;a&lt;/sup&gt;</td>
<td>.810</td>
<td>-.711</td>
<td>.016873463</td>
<td>R Square Change</td>
</tr>
<tr>
<td>1</td>
<td>.810</td>
<td>.533</td>
<td>8</td>
<td>1</td>
<td>.792</td>
</tr>
</tbody>
</table>

As shown above, the coefficient determination is 0.810. This implies that 81.0% of the variation in the financial ratio of return on assets (ROA) was explained by audit committee size, number of non-executive directors, number of board meetings, number of board committees, board diversity, the percentage of government ownership, the percentage of foreign ownership, and board size. This implies that there exists a negative relationship between the independent variables and financial outcome of commercial banks listed by the central bank of Kenya. As shown in the regression model, R square and adjusted R is high; therefore, this implies that there is a high variation that can be explained by the model.
Table 3: ANOVA for ROA

<table>
<thead>
<tr>
<th>Model</th>
<th>Sum of Squares</th>
<th>Df</th>
<th>Mean Square</th>
<th>F</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Regression</td>
<td>.001</td>
<td>8</td>
<td>.000</td>
<td>.533</td>
<td>.792</td>
</tr>
<tr>
<td>Residual</td>
<td>.000</td>
<td>1</td>
<td>.000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>.001</td>
<td>9</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

According to regression model above, the findings indicate that the predictors variable: number of audit committee meetings, percentage of government ownership, audit committee size, number of non-executive directors, number of board committees, percentage of foreign ownership, board diversity and number of board meetings, contributed to the overall relationship with the dependent variable, return on asset after controlling for bank size. The regression model shows an F-statistic of 0.533 and probability ratio (sig. F change) of 0.792. This means that independent variables were not significant in explaining the variation in the dependent variable (ROA).

Table 4: ROA Coefficients

<table>
<thead>
<tr>
<th>Model</th>
<th>Unstandardized Coefficients</th>
<th>Standardized Coefficients</th>
<th>T</th>
<th>Sig.</th>
<th>Correlations</th>
<th>Collinearity Statistics</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>B</td>
<td>Std. Error</td>
<td>Beta</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(Constant)</td>
<td>.342</td>
<td>.264</td>
<td>1.300</td>
<td>.418</td>
<td></td>
<td></td>
</tr>
<tr>
<td>board size</td>
<td>-.035</td>
<td>.032</td>
<td>-4.548</td>
<td>-.740</td>
<td>-.267</td>
<td>.011</td>
</tr>
<tr>
<td>number of board meetings</td>
<td>-.002</td>
<td>.007</td>
<td>-.518</td>
<td>-.729</td>
<td>.827</td>
<td>.055</td>
</tr>
<tr>
<td>number of board committees</td>
<td>.010</td>
<td>.010</td>
<td>1.153</td>
<td>.491</td>
<td>-.193</td>
<td>.151</td>
</tr>
<tr>
<td>board diversity</td>
<td>-.009</td>
<td>.017</td>
<td>-.771</td>
<td>.491</td>
<td>-.300</td>
<td>.082</td>
</tr>
<tr>
<td>number of non-executive directors</td>
<td>.022</td>
<td>.023</td>
<td>3.121</td>
<td>.503</td>
<td>-.358</td>
<td>.019</td>
</tr>
<tr>
<td>percentage of government ownership</td>
<td>-.007</td>
<td>.002</td>
<td>.000</td>
<td>1.000</td>
<td>-.599</td>
<td>.090</td>
</tr>
<tr>
<td>percentage of foreign ownership</td>
<td>.000</td>
<td>.001</td>
<td>1.041</td>
<td>.615</td>
<td>.017</td>
<td>.084</td>
</tr>
<tr>
<td>audit committee size</td>
<td>-.041</td>
<td>.036</td>
<td>-2.334</td>
<td>.457</td>
<td>-.194</td>
<td>.046</td>
</tr>
</tbody>
</table>

According to beta coefficient results, ROA has a positive relationship with the number of board committees (beta value of 1.027), number of non-executive directors (beta value 0.990) and percentage of foreign ownership (beta value of 0.690). The variables which were found to have a negative relationship with ROA included: number of board meetings, board diversity, the percentage of government ownership and audit committee. In general, the study found that the: number of audit committee meetings, the percentage of government ownership, audit committee size, number of non-executive directors, number of board committees, the percentage of foreign ownership, board diversity and number of board meetings were not statistically significant at 5% significant level. This implies that as the asset base of commercial banks in Kenya increases ROA as a performance measure increases
while changes in the board of directors, ownership structure and audit committee structure do not have any effect on ROA.

**ROE as a Dependent Variable**

The study adopted multiple regressions in testing whether there was a significant relationship between independent and dependent variables in order to meet the objectives of the study. Financial performance among listed commercial banks in Kenya was measured by Return on Equity (ROE). A multiple regression model utilized the relevant available data on the dependent and independent variables from 10 commercial banks listed by the Central bank of Kenya. The dependent variable (financial performance) was measured using the financial ratio of Return on Equity (ROE) and the independent variables relating to Board size, number of board meetings, number of board committees, board diversity, number of executive directors, number of non-executive directors, the percentage of government ownership, the percentage of foreign ownership, audit committee size and number of audit committee meetings.

The multiple linear regression model structure can be summed up as:

\[ FP = \beta_0 + b_1BOD_{1t} + b_2OWNS_{2t} + b_3ACS_{3t} + e_t \]

Where:  
FP = ROE  
\( \beta_0 \) = Regression constant to be estimated  
\( \beta_1 \) to \( \beta_4 \) = Regression coefficients to be estimated  
BOD\_t = Board of Directors (Board size, board meetings, number of board committees, number of executive and non-executive directors and board diversity)  
OWNS\_2 = Ownership Structure (percentage government ownership and foreign ownership)  
ACS\_3 = Audit Committee structure (audit committee size and number of audit committee meetings)  
e = Error /Disturbance Term

**Table 5: Regression Results for ROE**

<table>
<thead>
<tr>
<th>Model</th>
<th>R Square</th>
<th>Adjusted R Square</th>
<th>Std. Error of the Estimate</th>
<th>R Square Change</th>
<th>F Change</th>
<th>df1</th>
<th>df2</th>
<th>Sig. F Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>.894</td>
<td>.800</td>
<td>-.800</td>
<td>.10010483</td>
<td>.800</td>
<td>.500</td>
<td>8</td>
<td>.805</td>
</tr>
</tbody>
</table>

As shown in the table above, the coefficient determination is 0.800. This implies that 80.0% of the variation in the financial ratio of return on assets (ROE) was explained by audit committee size, number of non-executive directors, number of board meetings, number of board committees, board diversity, the percentage of government ownership, the percentage of foreign ownership, and board size. This implies that there exists a negative relationship between the independent variables and financial outcome of commercial banks listed by the central bank of Kenya. As shown in the regression model, R square and adjusted R of is high; therefore, this implies that there is a high variation that can be explained by the model.
Table 6: ANOVA Results for ROE

<table>
<thead>
<tr>
<th>Model</th>
<th>Sum of Squares</th>
<th>Df</th>
<th>Mean Square</th>
<th>F</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Regression</td>
<td>.040</td>
<td>8</td>
<td>.005</td>
<td>.500</td>
<td>.805</td>
</tr>
<tr>
<td>Residual</td>
<td>.010</td>
<td>1</td>
<td>.010</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>.050</td>
<td>9</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

According to regression model above, the findings indicate that the predictors variable: number of audit committee meetings, percentage of government ownership, audit committee size, number of non-executive directors, number of board committees, percentage of foreign ownership, board diversity and number of board meetings, contributed to the overall relationship with the dependent variable, return on asset after controlling for bank size. The regression model shows an F-statistic of 0.500 and probability ratio (sig. F change) of 0.805. This means that independent variables were not significant in explaining the variation in the dependent variable (ROE).

Table 7: ROE Coefficients

<table>
<thead>
<tr>
<th>Model</th>
<th>Unstandardized Coefficients</th>
<th>Standardized Coefficients</th>
<th>T</th>
<th>Sig.</th>
<th>Correlations</th>
<th>Collinearity Statistics</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>B</td>
<td>Std. Error</td>
<td>Beta</td>
<td>.514</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(Constant)</td>
<td>1.497</td>
<td>1.564</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>board size</td>
<td>-.154</td>
<td>.190</td>
<td>-.342</td>
<td>-.807</td>
<td>-.027</td>
<td>-.628</td>
</tr>
<tr>
<td>number of board meetings</td>
<td>.008</td>
<td>.043</td>
<td>.341</td>
<td>.180</td>
<td>-.530</td>
<td>.177</td>
</tr>
<tr>
<td>number of board committees</td>
<td>.054</td>
<td>.058</td>
<td>.107</td>
<td>.931</td>
<td>-.184</td>
<td>.681</td>
</tr>
<tr>
<td>board diversity</td>
<td>-.114</td>
<td>.102</td>
<td>-.175</td>
<td>.120</td>
<td>-.403</td>
<td>-.746</td>
</tr>
<tr>
<td>number of non-executive directors</td>
<td>.108</td>
<td>.135</td>
<td>2.598</td>
<td>.803</td>
<td>-.156</td>
<td>.626</td>
</tr>
<tr>
<td>percentage of government ownership</td>
<td>-.003</td>
<td>.013</td>
<td>-.385</td>
<td>-.258</td>
<td>-.475</td>
<td>-.250</td>
</tr>
<tr>
<td>percentage of foreign ownership</td>
<td>.004</td>
<td>.003</td>
<td>1.679</td>
<td>1.086</td>
<td>.007</td>
<td>.736</td>
</tr>
<tr>
<td>audit committee size</td>
<td>-.200</td>
<td>.211</td>
<td>-.197</td>
<td>-.945</td>
<td>-.297</td>
<td>-.687</td>
</tr>
</tbody>
</table>

Overall regression model: Fitted model \( FP = 1.497 - 0.098BOD_1 - 0.0001OWNS_2 - 0.200AC_3 \)

Discussion of Findings

Board of Directors and Financial Performance of Commercial banks

According to the regression analysis, ROA had a positive relationship with the number of board committees (beta value of 1.027) and number of non-executive directors (beta value 0.990) while regression analysis with ROE found a positive relationship with the number of board meetings (beta value of 0.180), number of board committees (beta value of 0.931), and number of non-executive directors (beta value 0.803). On the other hand, board size, number of executive directors and board diversity were negatively related with ROA and ROE. These findings are consistent with the findings of Taghizadeh and Saremi (2013) who also obtained a negative relationship between board diversity and the performance measures. Puni (2015)
results also indicated that board committees had no statistically significant effect on the corporate financial performance of listed firms which is consistent with the findings of the study. The findings are also consistent to those of Hermalin and Weisbach (2001) who observe that large boards consume a lot of time in the decision-making process because it is difficult to arrive at a consensus and they lack cohesiveness. Thus, the problem of coordination outweighs the advantages of having more board members. When boards consist of too many members, agency problems may increase because some board members may tag along as free riders thus hampering organizational performance (Haniffa & Hudaib, 2006). Conversely, according to Dalton and Dalton (2005), small boards may lack the advantage of having the spread of expertise, experience, and representation.

Ownership Structure and Financial Performance of Commercial banks
The regression model found a positive relationship between the percentage of foreign ownership with both ROA and ROE (beta value of 0.690 and 1.086 respectively). However, the percentage of government ownership had a negative relationship with both ROA and ROE. These findings are consistent with Chege (2013) who found a positive relationship between profitability and foreign shares ownership among commercial banks listed on the Nairobi Stock Exchange which according to Avulamusi (2013) was due to high monitoring capabilities of foreign owners. Similarly, Lin and Zhang (2009) found that banks partly acquired by foreign companies are more successful than those which kept their ownership structures. Hence, aligning the interests between principals and agents resolves for the agency problem and achieves the main goal of the shareholders, which is value maximization, consequently affecting firm performance positively. This is supported by Pallathitta (2005) who argued that foreign ownership goes beyond financial contribution and extends to provision of managerial expertise and technical collaboration which helps them to increase the efficiency and effectiveness of the operational processes leading to improved performance.

Audit Committee Structure and Financial Performance of Commercial banks
The study found that audit committee size had a negative relationship with both ROA and ROE (beta value of -1.145 and -0.945 respectively) while number of audit committee meetings was found to be positively related with both ROA and ROE. These results are supported by Amer, Ragab, and Shehata (2014) who also concluded that the audit committee size cannot influence firm’s financial performance, but found a positive association between number of audit committee meetings and the accounting-based performance measures (ROA and ROE). The findings are also supported by DeZoort et al, (2002) who proposed that a company where the audit committee met more frequently was likely to be more careful in safeguarding the interest of its investors. Also, it has been argued by Menon and Williams (1994) that for audit committees to be effective monitors, it is not enough just to be independent and that they must be active. Active could be measured by the frequency of their meetings. Morrissey (2000) suggests four meetings in a year for audit committees.

Conclusion
From the findings, it is evident that the study has revealed a number of critical issues as regards corporate governance practices in the Kenyan banking industry. The study concludes that there is a negative and significant relationship between Board of Directors, ownership structure and audit committee structure with the financial performance of listed commercial banks in Kenya in terms of ROA and ROE. Specifically, the study concludes that number of board committees, number of non-executive directors, percentage of foreign ownership and number of audit committee meetings have a positive impact on the financial performance of
commercial banks while audit committee size, board size, government ownership and board diversity have a negative impact on financial performance of listed commercial banks. Therefore, if commercial banks in Kenya are to improve their performance they should direct their efforts towards other variables other than board size, audit committee size, and board diversity.

**Policy Recommendations**

Based on the findings of this study, the researcher presents recommends the following policy actions towards addressing the gaps identified by the study. The study findings revealed that board size, board diversity and number of executive directors had a negative relationship with the financial performance of banks. Therefore, it is imperative that corporate board structure should be based on skills, experience and professional qualifications to improve the performance of banks. Requirements for one to be elected to the board of directors could be well stipulated in terms of features such as creativity, decision-making skills, and business ethics. The study findings showed that in a majority of the listed commercial banks in Kenya, board size was almost similar. For commercial banks to perform, board size should be hinged on the bank’s capital. This will improve efficiency and cut down operational costs.

**Areas for further research**

Due to limited time and resources, the study couldn’t exhaust the subject on how corporate governance structures influence financial performance of listed commercial banks in Kenya. This study did not consider all the corporate governance variables nor did it consider other non-accounting based measures to measure performance. Further research should also consider other diverse variables such as managerial ownership, capital structure, and disclosure that could not be included in this study. The researcher only considered ROA and ROE as a measure of firm performance. Measurement of firm performance cannot rely on only accounting based measures as was the case here. Further research can utilize market-based measures such as Tobin’s q to measure performance. Further research could also consider including other control variables apart from firm size, such as the age of the firm and leverage.

**References**


**About the Authors**

**Benedicta K. Kamazima** is currently working as a Management Associate at Citibank Tanzania. She holds an MBA (double major) in Financial Management and Strategic Management as well as a Bachelor of Commerce (Finance Major) from the Catholic University of Eastern Africa in Nairobi, Kenya. In addition, she has a Certified Investment and Financial Analyst (CIFA) Part III Section Five qualification.

Email: benedictakamazima@gmail.com

**Dr. Paul Mathenge** is a member of the Doctoral Association of Eastern Africa (DAEA), lecturing entrepreneurship. Implemented International trade centre objectives of empowering small scale entrepreneurs, and is currently working with the DAEA in mentoring upcoming researchers in this field.

Email: mathenge_paul@yahoo.com

**Dr. Thomas Katua Ngui** is a Lecturer at The Catholic University of Eastern Africa, Kenya. He has previously served as the Head of Department of Marketing and Management and also as Director Graduate Business School for the last eight years. He has published widely in the areas of Human Resources Management, Entrepreneurship, and Corporate Governance. Dr. Ngui is also a Director and Chairman of Finance and General Purpose Committee at Machakos Water and Sewerage Company Limited.

Email: nguitom@yahoo.com
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