THE RELATIONSHIP BETWEEN CORPORATE GOVERNANCE PRINCIPLES AND FINANCIAL PERFORMANCE OF INVESTMENT BANKS IN THE NAIROBI SECURITIES EXCHANGE

KAMWARO KELLEN NYAGUTHII

A Research Project Submitted To the School Of Business in Partial Fulfilment for the Award of Degree in Master of Business Administration, Egerton University (Finance Option)

EGERTON UNIVERSITY

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DECLARATION AND APPROVAL

DECLARATION

This Research Project is my original work and has not been submitted for a degree qualification in any other university or institution of higher learning.

SIGNED.. DATE......................................

KAMWARO KELLEN NYAGUTHII

CM16/0237/12

SUPERVISOR'S APPROVAL

This Research Project has been submitted for Examination with my approval as the University Supervisor.

SIGNED.. DATE...............................

DR. FREDRICK M. KALUI

Senior Lecturer, Department of Accounting, Finance and Management Science

Faculty of Commerce

Egerton University

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DEDICATION

I hereby dedicate this research project to the Almighty God, to my parents Mr and Mrs Kamwaro and fiancé Pln. Wallace G. Mochu, for their inspiration and unwavering encouragement.

ACKNOWLEDGEMENT

I am indebted to the Almighty God for the gift of life and sound health that has been sufficient this far. I extend the same to Egerton University for giving me the opportunity to pursue a master's programme in Business Administration. Special thanks to my supervisor, Dr. Kalui for the invaluable insight in the proposal and project formation. I am grateful to all teaching, administrative and support staff of the Egerton University for the support during the period. I acknowledge the administration and staff of HELB postgraduate studies for the scholarship award that supported the studies to completion. I extend my acknowledgement to my classmates for the guidance and invaluable resources in this pursuit. My parents, siblings, friends and fiancé thank you for the continued support.

ABSTRACT

Corporate governance is an area that has grown rapidly in the recent years as an emerging issue due to the global corporate scandals and collapse of big companies. The corporate governance principles hence adopted by any corporate entity affects the firm's ability to respond to the content and context in which it operates and its overall performance. The purpose of this study was to assess the relationship between corporate governance principles and financial performance of investment banks in the Nairobi Securities Exchange. The objectives of the study were to investigate the relationship between corporate governance principle aspects (board composition, CEO duality, board size principles) and ROA of investment banks in the Nairobi Securities Exchange. The study used a descriptive research design where primary data was collected from the seven investment banks in the Nairobi Securities Exchange in Nairobi County using a questionnaire issued to the managers while secondary data was in the form of published financial statements. Statistical Packages for Social Sciences (SPSS) was used by the researcher to facilitate the analysis and interpretation of data and the results obtained was presented using tables, frequencies, graphs and charts for easy interpretation. The correlation results indicated that the corporate governance principles (CEO duality and Board composition) had a strong negative correlation on financial performance in investment banks while board size had a weak negative correlation on financial performance in investment banks. The regression analysis showed that CEO duality, board composition, board size and their combined contribution had a significant effect on the financial performance in investment banks.

The study recommends that investment banks operations were to be governed through a clear management structure that enhances security of shareholder wealth and sustainability of the organisation. This is to be achieved by continually reviewing regulations regarding management governance structures so as to assure transparency in limiting CEO duality thus assuring legitimacy in the firm performance. The board members in investment banks should entail a pool of diverse skills and expertise to enhance innovative ways in steering business performance. This could be enhanced through independent recruitments from a pool of experts and the pre-allocation of equitable balance in the boards and the board member number should be maintained on an optimal basis of five or less. The study purpose thus

requires institutions to invest in the optimal operationalization of the corporate governance focused in this study.

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LIST OF ABBREVIATIONS

CEO Chief Executive Officer

CMA Capital Markets Authority

IPO Initial Public Offer

IFRS International Financial Reporting Standards

KASIB Kenya Association of Stock brokers and Investment Bank

KBA Kenya Bankers Association

MIS Management Information System

NSE Nairobi Securities Exchange

NSSF National Social Security Fund

OECD Organisation for Economic Co-operation and Development

PwC PricewaterhouseCoopers

RBA Retirement Benefits Authority

ROA Return on Assets

SOX Sarbanes-Oxley Act

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CHAPTER ONE

INTRODUCTION

1.1 Background of the study

Corporate governance entails a set of relationships between a company's management, its board, its shareholders and other stakeholders. It further provides the structure through which the objectives of the company are set and the means of attaining those objectives and monitoring performance. Therefore, the attainment of the objectives and monitoring performance has wider implications that are critical to economic and social well-being. This is through the provision of the requisite incentives and performance measures to achieve the predetermined business success as well as to enhance the stewardship of the resources through transparency to ensure the equitable distribution of the resulting wealth (OECD, 2009).

The corporate governance principles hence adopted by any corporate entity affects the firm's ability to respond to the content and context in which it operates and its overall performance. It is thus evident that well governed firms perform better to a greater extent than poorly governed ones hence the need of appropriate corporate governance principles. A sound corporate framework benefits firms through greater access to financing, lower cost of capital, better financial performance and more favourable treatment of all stakeholders. They argue that weak corporate governance leads to poor firm financial performance and risky financing patterns (Claessens et al., 2002).

Corporate governance has been a major policy reform and discussion in Kenya for over a decade evidenced by corporate governance guidelines issued by the Capital Markets Authority and supported by private sector initiatives, including widespread director training, improving governance across listed companies. Revived privatization, performance contracts, vetting of state officers, establishment of independent commissions and other reforms have placed increasing emphasis on the corporate governance of state corporations, which continue to play a major role in the economy. Kenya recognizes the value of good governance as demonstrated in the constitution in Chapter 2 article 10 (1) on National Values and Principles

of Governance commits all persons, state organs and any other parties to the national values, good governance being one of the values (Capital Markets Authority, 2014).

Investment banks entail financial institutions that deal mainly with corporate and retail customers with specialisation in securities markets activities including underwriting, trading, asset management, advisory activities and corporate restructuring such as mergers and acquisitions. They thus play a vital role in assisting mid-market businesses maximize value. The key success factor for the development of such investment banks in the developed world has been their access to capital in their own right, thus enabling them to make the guarantee in the first place. However, the existence of major scandals in these developed countries in the past brought about the much needed corporate governance for institutions to incorporate (Marks, 2012).

Enron, one of America's largest energy corporations incurred tremendous financial losses as a result of arrogance, greed and foolishness from the top management to the bottom of the pyramid. The hiding of financial losses of the trading business and other operations through a market to market practice was designed to make the company appear to be more profitable than it really was .In South East Asia, Refco one of America's largest futures brokers defrauded investors in the firm's initial public offering by hiding hundreds of millions of dollars in loans to another company. This was spearheaded by the CEO(Chief Executive Officer) in a company he had control in a scheme to hide as much as 545 (five hundred and forty five) million dollars having cleverly repaid the money just before routine audits (Seabury, 2011).

In Kenya, Francis Thuo and Partners went under in early 2007, marking the first of a series of stockbroker failures that were largely blamed on weak management and fraudulent selling of investors' shares by the intermediaries. Nyagah stockbrokers were put on statutory management in 2008 after failing to meet its financial obligations. In addition, a forensic audit done by PricewaterhouseCoopers (PwC) revealed that the firm might have gone down with about Shs1.3billion of public funds through the diversion of funds by management, fraud by the staff, occurrences of collusion by other stockbrokers in the NSE and even office of the regulator (CMA, 2014).

An RBA (Retirement Benefits Authority) report in 2012 disclosed that NSSF (National Social Security Fund) had investments in shares through Discount Securities amounting to

over Sh. 15 billion which was a thirty-four per cent of NSSF assets. Discount Securities, which was one of the brokers, disbursed the funds used in the purchase of shares in more than 80 nominee accounts through which it invested NSSF money in the stock market. NSSF issued cheques to the broker to facilitate the purchase which on calculation was worth more than Sh15 billion whereas the share certificates issued were worth Sh.14.3 billion. This culminated to the broker facing criminal charges for non-delivery of share certificates worth more than Sh1 billion as well as failing to pass on dividends payable to NSSF worth over Sh100 million.

The financial sector in Kenya has in the recent past been subjected to corporate governance credibility over management and supervision of the banks in this sector. This has been evidenced by the cases of bank failures from Dubai, Imperial, National and Chase banks. The auditors and regulators of these institutions colluded through the misrepresentation of the financial position so as to make the institutions to be deemed profitable, evade tax and under report debt. The financial results show the financial soundness of the company which is crucial in determining the investor and employee confidence thus the cover up of the malpractices in such information constituted to their tumbling down (Achuka, 2016).

Corporate governance has therefore emerged as a major policy concern for many developing countries following the financial crisis in Asia, Russia, and Latin America. The collapse of Enron suggests that even the highly industrialized countries such as the U.S. are not immune to the disastrous effects of bad corporate governance. Studies have shown that low corporate governance standards raise the cost of capital, lower the operating performance of industry, and impede the flow of investment (Gatamah, 2004).

In light of the size of the Kenyan economy and its vision in the blueprint of Vision 2030, it will take financial institutions like investment banks to provide the backing for large IPO (Initial Public Offer) and bond issues. Strong corporate governance will thus be indispensable to resilient and a vibrant capital market as an important instrument of investor protection since business enterprises that do not prosper lead to employment decline, tax revenue falls and invariable economic growth hindered. Good corporate governance, therefore, becomes a prerequisite for national economic development (Dave, 2009).

1.2 Statement of the problem

The financial scandals around the world and the recent collapse of major financial institutions in USA, South East Asia and Kenya have shaken investors' confidence in the capital markets. Capital Markets Authority of Kenya (CMA) the regulatory body in the capital market has key interests on the shareholders who invest in the quoted companies so as to determine the value for the investment is maximised. Corporate governance therefore, receives high priority on the agenda of policymakers, financial institutions, investors, companies and academics (Heracleous, 2001).

Corporate governance has received much attention in the academic literature with a number of studies having sought to investigate the relation between corporate governance mechanisms and financial performance (Berglof & Thadden, 1999). Most of the studies have shown mixed results without a clear-cut relationship. A study by Becht et al. (2002) indicated that corporate governance practices positively influences the profitability of the organization while MacAvoy and Millstein (2003) found that board composition does not have any effect on financial performance. Further, the limited studies in the area have focused mainly on developed economies. It is therefore crucial to examine the relationship in the context of a developing economy.

Studies done locally regarding corporate governance have majored on public institutions, the private institutions and the listed companies. Maulu (2014) carried out a study on the relationship between corporate governance and financial performance of stock brokerage firms and investment banks in Kenya. The findings were that a relationship exists between different aspects of corporate governance practices and financial performance with firms having bigger boards reporting better results than those with small ones and that no significant relationship between ownership structure, information disclosure and frequency of meeting with financial performance of firms. Ada B. (2013) conducted a study on the relationship between corporate governance practices and dividend pay-out of commercial banks in Kenya. The findings were that 72.7% of dividend pay-out in the commercial banks was positively related to corporate governance practices that had statistically significant values. Miring'u, A. and Muoria, E. (2011) carried out a study to examine corporate governance effects on the performance in commercial state corporations in Kenya. It was

identified that a positive relationship exists between Return on Equity (ROE) and board size and board compositions of all state corporations.

None of these studies have focused on the relationship between board composition, board size and CEO duality and Return on Assets (ROA) of investment banks in the NSE. Investment banks occupy a special place due to their centrality in the transmission of monetary policy and the functioning of the payment and settlement systems. There is need to determine whether corporate governance principles influence their financial performance. Therefore based on the limited empirical data and the great exposure of such institutions in the financial sector this study sought to provide more empirical data in Kenya.

1.3 Purpose

To assess the relationship between corporate governance principles and financial performance of investment banks in the NSE.

1.4 Objectives

i. To establish the relationship between board composition and ROA of investment banks in the NSE.
ii. To determine the relationship between CEO duality and ROA of investment banks in the NSE.
iii. To determine the relationship between board size and ROA of investment banks in the NSE.

1.5 Research Hypotheses

Ho_1; there is no relationship between board composition and ROA of investment banks in the NSE.
Ho_2; there is no relationship between CEO duality and ROA of investment banks in the NSE.
Ho_3; there is no relationship between board size and ROA of investment banks in the NSE.

1.6 Significance

Most research studies have concentrated on the effects of corporate governance principles on the financial performance of stock brokers and parastatals but little has been done primarily

on investment banks. The study will enhance management adoption and implementation of corporate governance principles in investment banks that are the custodians of the shareholder funds for the ultimate accomplishment of corporate goals.

1.7. Justification of the Study

The study findings are invaluable to the shareholders who invest in such companies so as to determine the value for the investment made based on the level of expertise of management with the appropriateness of measures requisite for mitigating unforeseen losses .The study findings further provide the government with a framework on developing appropriate measures in safeguarding the investors while guiding investment banks.

1.8 Scope of the Study

The scope of the study consisted of the financial institutions operating wholly as investment banks licensed by the CMA in the Nairobi Securities Exchange within Nairobi County. The total of these institutions was seven with a high presence of branches in Nairobi County. The management staff in the various branches provided the information due to their position in the institutions that was relied upon by the researcher.

The corporate governance principles as the independent variables focused in the study were board composition, board size and CEO duality while the financial performance measure for the study as the dependent variable was the return on assets (ROA).The secondary data was based on the published financial statements such as statement of financial position, statement of financial performance and the cash flow for the period 2010 to 2013.

1.9 Limitations of the Study

The study encountered various limitations that hindered access to information. The main limitation of the study was some respondents being reluctant to reveal information that was considered confidential and were unwilling to share the information. The researcher, therefore, took the necessary steps and measures to ensure that proper communication was made on the purpose of the study and assured the respondents of confidentiality of information provided.

Literature relating to the developing investment banking in developing nations such as Kenya is limited. This was mitigated by assessing the audited published reports on financial performance and corporate governance processes for the companies concerned.

1.10 Definition of Operational Terms

***Board Expertise*;** this entails the pool of skills and experience of the board members relating to the managing of financial institutions resources.

Board Composition; this refers to the pool of skills, gender and expertise of board members in an organisation.

Board Size; this refers to the number of individuals chosen to constitute the board in an organisation.

Capital; this refers to the money, property and other valuables which collectively represent the wealth of an individual or business and available for a particular purpose.

CEO Duality; this is the holding of the roles of Chairman and CEO position by a single individual in an organisation.

Corporate Governance Principles; this is a set of processes and policies affecting the way a corporation is administered through the distribution of rights and responsibilities among that work in an organisation

Investment; this is a monetary asset that is purchased with the hope that it will provide income in future or appreciate and sold for a higher value.

Investment Bank; this is a financial institution that specialises in securities markets activities such as underwriting, trading, asset management, advisory activities and corporate restructuring

Investor; this is an individual or entity that commits money to investment products with the expectation of financial return

Management Structure; this relates to the distribution of power within an organisation through respective tasks and responsibilities assigned.

Management Expertise; this refers to the pool of the professionals within the board of management that provides insight in the operations of the core functions.

Optimal Size; this refers to the appropriate number of board members based on guidelines within or outside the institutions' environment.

Proactive; this entails measures undertaken by management to mitigate the chances of a negative outcome against the predetermined strategies.

Return on Assets; this is a measure of financial performance of what income is attributable to an institution's assets.

Transparency; this is the attribute of openness in dealings relating to mutual relationships among individuals within predetermined contracts.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

This chapter summarizes the information from other researchers who have carried out their research in the same field of study. The specific areas covered here are corporate governance principles; board composition, CEO duality and board size, investment banks, Return on Assets (ROA), theoretical review; Stewardship theory, Stakeholders theory, Agency theory, empirical review and conceptual framework.

2.2 Corporate Governance Principles

Corporate governance refers to the way in which organisations are directed and controlled. It further defines the relationships and the distribution of rights and responsibilities among

those who work with and in the organisation. It determines the conditions for access to capital markets and degree of investors' confidence (Brownbridge, 2000).

It determines the rules and procedures through which the organisation's objectives are set and provides the means of attaining those objectives and monitoring performance. Importantly, it defines where accountability lies throughout the organisation (Dipple, 2011). Corporate governance is both the promise to repay a fair return on capital invested and the commitment to operate a firm efficiently given investment from the perspective of the investor (Metrick & Ishii, 2002).

Good corporate governance practices ensure integrity, transparency, accountability and enforceability in the market place. (Tapscott &Ticoli, 2001) They facilitate efficient allocation of resources and guarantee investors substantial returns on their investment. Corporate governance further enhances investor protection and encourages investment (Yeo, 1999). The principal players are the shareholders, management and the board of directors while other stakeholders include employees, suppliers, customers, banks, regulators, the environment and community at large (Knell, 2006).

These ideals are necessary for any country in order to attract investors both local and foreign and assuring efficient management and security of their investments in a transparent and accountable process. It further promotes competitive and efficient companies and business enterprises by enhancing the accountability and performance of those entrusted to manage corporations. Efficient companies or business enterprises in the country are able to create employment and wealth. In retrospect, the lack of investment in companies leads to stagnation and collapse (Yeo, 1999).

Kenya's corporate governance has in recent times been put in question with revelations that the financial malpractices were being done in several companies including CMC Holdings, Mumias Sugar and Kenya Airways under the watch of external auditors. The financial sector has also been subjected to corporate governance credibility over management and supervision of the banks in this sector. This has been evidenced by the cases of bank failures from Dubai, Imperial, National and Chase banks. The auditors and regulators of these institutions colluded through the misrepresentation of the financial position so as to make the institutions to be deemed profitable, evade tax and under report debt. The financial results show the financial

soundness of the company which is crucial in determining the investor and employee confidence thus the cover up of the malpractices in such information constituted to their tumbling down (Achuka, 2016).

Capital Markets Authority in Kenya is primarily responsible for regulating its members and listed companies through its various rules and regulations. A major role is in monitoring and enforcing continuing listing obligations, which are geared towards ensuring comprehensive and timely disclosure, particularly of material information pertaining to the performance of listed companies. The mission to institutionalize principles of corporate governance in Kenya culminated in the promulgation of the Guidelines on Principles of Corporate Governance for Public Listed Companies in the CMA 2014 framework. The Guidelines encourage listed companies to embrace a positive corporate culture of accountability and responsiveness to the interests of investors. The fact that non-compliance with the guidelines is largely inconsequential was intended to engender them to listed companies (CMA, 2014).

2.2.1 Board Composition Principle

The composition of the board may be used to address the principal-agent problem. The participation of outside directors is designed to enhance the ability of the firm to protect itself against threats from the environment and align the firm's resources for greater advantage. Firms with higher number of outside directors are expected to pursue activities that would bring about low financial leverage with a high market value of equity. An adherence to the gender ratio in determining the board composition enhances mutual relationships and diversity of management views (Baysinger & Butler, 1985).

The supervisory committee of companies are largely technical and would be appropriate if at least one of the people elected to it has some experience or training in auditing or book-keeping. It is from whoever has some knowledge that the other members of the committee can be guided. Independence of committees is also considered important for a board committee to be an effective monitor. Boards should be ready to increase meetings frequency if the situation requires a high supervision and control (Shivdasani & Zenner, 2004).

Jensen (1993) held that the board of directors is assumed to have an influence on performance since it is vested with responsibility for managing the firm and its activities. The board is composed of the executive directors and non-executive directors (Shah et al., 2011). The executive directors are termed to as dependent and have insider information of the organisation. The non-executive directors constitute the independent board composed of members who have no ties to a firm thus limited conflict of interest due to no material interest (Gallo, 2005).

2.2.2 CEO Duality

The Chief Executive Officer (CEO) of an organisation through the corporate governance provisions in the firm can create value for the shareholders (Defond & Hung, 2004). The decisions of the board about hiring and firing a CEO and their proper remuneration have an important bearing on the value of the firm. The board terminates the services of an underperforming CEO who fails to create value for shareholders. It is the responsibility of the board to determine the salary of the CEO and give proper remuneration for their efforts. This can be by aligning the firm performance and their salary since their financial interests are attached to the firm performance (Monks & Minow, 2001).

The tenure of a CEO is an important determinant of firm performance. CEOs hired on short term contracts are more concerned about the performance of the firm during their tenure by laying emphasis on short and medium term goals (Bhagat & Jefferis, 2002). The management of a firm can overcome this problem by linking some incentives for the CEO with long term performance of the firm (Heinrich, 2002). CEO duality plays an important role in affecting the value of a firm. A single person holding both the Chairman and CEO position role improves the value of a firm as the agency cost between the two is eliminated (Alexander, Fennel & Halpem, 1993). On the negative aspect, CEO duality leads to worse performance since the board cannot remove an underperforming CEO and can create an agency cost if the CEO pursues his own interest at the cost of shareholders (White & Ingrassia, 1992).

Individuals holding two top positions have a tendency on the path of adopting personal interests' strategies that could be detrimental to the firm. The combined roles that the chairman of the board has to decide lead to conflicting interests whereas the case of the CEO setting the board's agenda can influence the selection of the directors. This hence poses a

challenge on the board’s ability to monitor executives. The separating of the CEO and chairman roles is in the shareholders' interest. Similarly, large firms that separate the two functions trade at higher price-to-book multiples and have higher return on assets and cost efficiency ratios than firms where the same person holds both titles (Jensen & Meckling, 1976).

2.2.3 Board Size

The board of directors of an organization is a key mechanism to monitor managers’ behavior and advise them. The existence of larger boards is costlier than smaller boards based on ineffectiveness in communication, coordination of tasks and decision making. Limiting the board size to a particular level is widely believed to improve performance of the firm at all levels (Berle & Means, 1932).

Hermalin and Weisbach (2003) argued that larger boards constituting more than seven members can be less effective than small boards due to the increased agency problems that make a large board more of a symbolic role rather than fulfilling its intended function as part of the management. Small boards are preoccupied with decision making process though lack the advantage of having the spread of expert advice and opinion found in larger boards. Consequently, larger boards are more likely to be associated with an increase in board diversity in terms of experience, skills, gender and nationality (Dalton, 2009).

The right size for a board is not specific in all organisations since each board needs to define its optimal capacity at any given time. Certain considerations are of concern when determining the size of the board such as state legislation and organization by laws. In most states, the laws dictate the minimum size for non-profit boards and parastatals. The range is from three to seven board members that is required in executing organisational decision making. However, a small board with less than three members would rarely be able to incorporate a diverse view of perspectives and attributes necessary for a strategic based organization (Goss, 2013).The study will therefore base a small board size as constituting of five members or less while a large board size as constituting more than five members.

2.3 Investment Bank

A financial institution that deals mainly with corporate customers and specialises in securities markets activities including underwriting, trading, asset management, advisory activities and corporate restructuring such as mergers and acquisitions. It related to the creation of capital for other companies by underwriting new debt and equity securities for all types of corporations. Investment banks also provide guidance to issuers regarding the issue and placement of stock (CFA, 2014).

Dave (2009) sought to segment investment banking into four main categories that entail asset management, brokerage, corporate advisory and underwriting. Asset management entails a mutual fund that actively tracks stocks likely to make the highest return by providing 8724 products that track the value of other investments directly without actually being invested in that security such as an exchange traded fund.

In Kenya, active investment is an emerging trend by a small segment of investment banks with established players. The line of business is conducted through a separate subsidiary to avoid conflict of interest and closely regulated to ensure that asset managers are prudently managing funds alongside proper record keeping. The subsequent returns are made through a management fee of typically a range of 1% to 5 % of the assets. However, a number of Kenyan brokerages have in the past become active fund managers of funds that clients entrusted them but totally used for different purposes and as a consequence much hesitation to entrust such funds to fund managers. Therefore the need arose for a brokerage with a strong brand name to pursue this line of business. This has been an emerging trend in the developing countries by investment banks propelled by their client access, local knowledge, managerial capability and the capability to develop innovative financing solutions (Dave, 2009).

Brokerage entails the core execution of purchase and sale orders on the capital markets for a commission which has grown to be an exceptional revenue generator through commissions for banks that have ventured in this field. It further entails distribution of securities by acting as the primary seller during an IPO (Initial Public Offer). The final activities are market making in that to act as a seller or buyer of last resort for particular securities as well as proprietary trading through speculative activity in the markets. Brokerage has a range of functions to cater for the market needs. The provision of vital information through the trading

activity acts as the price signal in capital markets. It serves as an efficient basis of re-allocation of capital from one to another activity on a macroeconomic basis through individual transactions. The brokerage mitigates risk in the market by acting as a responsible custodian of clients' funds and counterparty to transactions hence reducing settlement risk (CMA, 2014).

The price signal function has faced allegations of market rigging and insider trading hence distorting the flow of information and dispels the notion of accurate prices. The reallocation of such capital can be effected through proper and timely execution of participants' decisions on whether to buy distributed new securities at a particular price, hold or sell existing securities, and finally remitting that capital to the owners. The inefficient administration further leads to failures to remit payments to clients and keep records with any accuracy, leading to debacles like the liquidity crunch following the Safaricom IPO. The reduction of such risk is achieved through both interfaces with the broker acting as a custodian and executor under the trust bestowed by the client. The accurate records maintenance, prompt and timely execution of orders could further enhance investor participation and wealth creation (NSE, 2007).

Corporate advisory entails a range of activities common in developed countries. It provides advice relating to financing, strategy, tax implications and balance sheet management for mergers and acquisitions. In view of balance sheet advisory, an optimal balance sheet structure is developed and delivered while taking into account the views of stakeholders, tax implications and costs of capital. For specialised advisory it is involved in areas of asset finance, hostile take-overs and tax structuring. It is therefore an emerging trend in developing countries like Kenya and accessible to large companies capable of drawing together complex teams of advisors. Investment banks therefore need to innovate and develop demand for their own advisory services that will reap them greatly (Dave, 2009).

Underwriting involves assuming a risk on behalf of an investor selling securities in the stock market. The company seeks an assurance that money is raised for the stock issued even when some shares have not been sold. Investment bankers place their capital risk by buying all the securities from the company at a discounted price. The investment banks then mark up the securities to market retail price and sell them to the investing public. If the sale of securities does not reach the target capital requirement, they are forced to borrow from commercial

banks or sell the shares at a loss. Alternatively, they also invite other investment banks to take part in the underwriting process to share the risk of loss in form of an underwriting syndicate (Petrick, 2013).

2.4 Return On Assets

This is a financial ratio that shows the percentage of profit that a company earns in relation to the overall resources (total assets). Return on assets is a key profitability ratio which measures the amount of profit made by a company per shilling of its assets thus shows the company's ability to generate profits before leverage, rather than by using leverage. It is a ratio of income to its total asset. In light of investment banks, it measures the ability of the management to generate income by utilizing company assets at their disposal efficiently as well as generating net income from all the resources of the institution (Khrawish, 2011).

ROA as per International Financial Reporting Standards (IFRS) is generally calculated as follows:

$$\text{Return on Assets (ROA)} = \frac{\text{Net Income}}{\text{Average Total Assets}}$$

Average Total Assets = (Beginning Total Assets + Ending Total Assets) / 2

The ROA offers a standard for assessing how a business management efficiently uses the average resources in the creation of business assets. This leads to the determination of the income derived from such business assets by potential and existing investors and further assess the management adherence to corporate governance principles. It therefore evaluates the business capacity to create profits prior to leverage through using the business assets. The ROA is thus a comparison of average total assets with the net income (Campbell, 2009).

ROA shows earnings that are generated from invested capital (assets). ROA for public companies can vary substantially and is industry-specific thus, when used as a comparative measure, it is best to compare it with a company's previous ROA numbers or the ROA of a similar company. A company's assets consist of both debt and equity, which are used to fund the operations of the company. ROA gives investors some idea of how effectively the company is converting the money it has into net income. The higher the ROA, the more the

company utilises resources efficiently unlike low returns that indicate inefficiencies (Scott, 2003).

The study was limited in scope on ROA as a performance measure since it is used internally by companies to track asset-use over time, to monitor the company's performance in light of industry performance and to look at different operations or divisions by comparing them one to the other. Therefore it is useful in comparing competing companies in the same industry. Effective corporate governance must be in place to allocate assets accurately to different operations in line with their capacities and potential (Bernstein et al., 2000).

2.5 Theoretical Framework

2.5.1 Agency Theory

Berle and Means (1970) developed this theory on the basis that the separation of ownership and control lacked sufficient checks upon autonomy of corporate managers. It has been pointed out as referring to that separation of control from ownership implying that professional managers manage a firm on behalf of the firm's owners (Kiel & Nicholson, 2003). According to this theory, people are self-interested hence cannot be trusted to act in the best interests of others. On the contrary, people seek to maximize their own utility with conflicts arising when a firm's owners perceive the professional managers not to be managing the firm in the best interests of the owners (Berle & Means, 1970).

The theory rests on the assumption that the role of organizations is to maximize the wealth of their owners or shareholders (Blair, 1995). However, most businesses operate under conditions of incomplete information and uncertainty hence expose businesses to two agency problems namely adverse selection and moral hazard. Adverse selection occurs when a principal cannot ascertain whether an agent accurately represents his or her ability to do the work for which he or she is paid to do. On the other hand, moral hazard is a condition under which a principal cannot be sure if an agent has put forth maximal effort due to different attitudes towards risk (Eisenhardt, 1989). The two problems hence bring about a particular type of management cost termed as agency costs that ensure that agents act in the principal's interests (Jensen & Meckling, 1976).

Berle and Means (1970) point out that superior information available to professional managers allows them to gain advantage over owners of firms. The reasoning is that a firm's top managers may be more interested in their personal development than in the welfare of the firm's shareholders. The theory therefore suggests that a firm's top management should have a significant ownership of the firm in order to secure a positive relationship between corporate governance and the amount of stock owned by the top management (Mallin, 2004). Carpenter and Westpal (2001) opine that the agency theory is therefore applied by boards of profit making organizations to align the interests of management with those of shareholders.

Donaldson and Davis (1991) argue that managers will not act to maximize returns of shareholders unless appropriate governance structures are implemented to safeguard the interests of shareholders. Therefore, the agency theory advocates that the purpose of corporate governance is to minimize the potential for managers to act in a manner contrary to the interests of shareholders. Jensen and Meckling (1976) hold that the agency theory is therefore concerned with aligning the interests of owners and managers and is based on the premise that there is an inherent conflict between the interests of a firm's owners and its management. This implies that the actions of directors, acting as agents of shareholders, must be checked to ensure that they are in the best interests of the shareholders

2.5.2 Stakeholder Theory

Ed Freeman (1980) developed this theory which sprouted from the premise that organizations serve a broader social purpose than just maximizing the wealth of shareholders. It holds that corporations are social entities that affect the welfare of many stakeholders where stakeholders are groups or individuals that interact with a firm and that affect or are affected by the achievement of the firm's objectives (Donaldson & Preston, 1995; Freeman, 1984).

Successful organizations are judged by their ability to add value for all their stakeholders. Some scholars consider the natural environment to be a key stakeholder (Starik & Rands, 1995; Dunphy et al., 2003). Stakeholders can be instrumental to corporate success and have moral and legal rights (Donaldson & Preston, 1995; Ulrich, 2008). Corporate leaders have to therefore consider the claims of stakeholders when making decisions (Blair, 1995) and conduct business responsibly towards the stakeholders (Manville & Ober, 2003; White, 2009). Participation of stakeholders in corporate decision-making can enhance efficiency and reduce conflicts (Rothman & Friedman, 2001)

According to Kaptein and Van Tulder (2003), corporations adopt reactive or proactive approaches when integrating stakeholders' concerns in decision making. A corporation adopts a reactive approach when it does not integrate stakeholders into its corporate decision making processes. This results into a misalignment of organizational goals and stakeholder demands (Mackenzie, 2007). Some authors attribute scandals such as those of Enron to the failure to consider stakeholder concerns in decision making (Currall & Epstein, 2003).

In line with these scandals, some governments set up new regulations to align the interests of stakeholders with corporate conduct. For example, the Sarbanes-Oxley Act (SOX) was passed as a result of the collapse of Enron. Adams (2002) argues that the theory remains the theoretical foundation for much regulation and legislation. A proactive approach is used by corporations that integrate stakeholders' concerns into their decision-making processes and that establish necessary governance structures (Wit et al., 2006). Dobson (1991) argues that the demands of profit making organizations are different from those of stakeholders such as shareholders, local communities, employees and customers. The conflicting demands can be used to justify actions that some may criticise as immoral or unethical depending on the stakeholder group.

2.5.3 Stewardship Theory

Donaldson and Davis (1991) developed this theory where they considered managers as good stewards who will act in the best interest of the owners. It is based on the behaviour of executives which is pro-organisational and has a higher utility than individualistic self-serving behaviour and does not depart from the interest of the organisation (Davis, Schoorman & Donaldson, 1997).

Smallman (2004) argues that where shareholder wealth is maximised the steward's utilities are maximised since organisational success will serve most requirements and the stewards will have a clear mission. This therefore implies that the theory exhibits a strong relationship between managers and the success of the firm hence stewards protect and maximise shareholders wealth through firm performance. Davis, Schoorman and Donaldson (1997) further hold that a steward who improves performance successfully satisfies most stakeholder groups in an organisation in turn steer organisational wealth.

The stewardship theory focuses on the structures that facilitate and empower rather than monitor and control hence a relaxed view of separation of the executives with support for majority of specialist executive directors rather than non-executive directors (Clarke, 2004). Stewards therefore seek to balance tensions between different beneficiaries and interest groups by satisfying their requirements resulting in dynamic performance equilibrium for balanced governance (Davis, Schoorman & Donaldson, 1997).

The study will therefore adopt the agency theory since it is based on a contract between the shareholders as the principal and board of directors or managers as the agents with the underlying objective of maximising returns on assets. The agency conflict that arises in this contract by the management acting in their own self-interest jeopardises the shareholders returns. This hence results in the shareholders incurring agency costs through the institutionalisation of corporate governance principles to mitigate the potential of managers acting in a manner contrary to the interests of shareholders.

2.6 Empirical Studies

Corporate Governance is the manner in which the power of a corporation is exercised in the running of the corporation's total portfolio of assets and resources with the objective of maintaining and increasing shareholder value and satisfaction of other stakeholders in the context of its corporate mission. A range of studies have embarked on research project on this concept over the years with the aim of getting more insight on what it entails. The various contributions made through their findings have been subject to scrutiny by the subsequent studies in this field.

Maulu (2014) carried out a study on the relationship between corporate governance and financial performance of stock brokerage firms and investment banks in Kenya. The study employed a casual research design where primary data was collected from 23 stock brokerage firms and investment banks licensed the NSE. The findings were that a relationship exists between different aspects of corporate governance practices and financial performance. The study also revealed that firms with bigger boards reported better results than those with small

ones and that no significant relationship between ownership structure, information disclosure and frequency of meeting with financial performance of firms.

Ada B. (2013) conducted a study on the relationship between corporate governance practices and dividend pay-out of commercial banks in Kenya. A correlational research design was employed for the 17 commercial banks in Kenya that had paid dividends between 2008 - 2012. The findings were that 72.7% of dividend pay-out in the commercial banks was positively related to corporate governance practices that had statistically significant values. Wanjiku et al (2011) carried out a study to establish the corporate governance practices of firms and its relationship with the growth of companies listed at the Nairobi Securities Exchange using a causal comparative research design. The study focused on corporate communication, leadership and technology application. The study found a positive linear dependence of growth and corporate governance.

Miring'u, A. and Muoria, E. (2011) carried out a study to examine corporate governance effects on the performance in commercial state corporations in Kenya. A descriptive research design was employed for 30 state corporations. It was identified that a positive relationship exists between return on equity (ROE) and board size and board compositions of all state corporations. Kavulya (2011) studied the relationship between corporate governance and financial performance of the deposit taking Savings and Credit Cooperatives in Kenya. The study employed a descriptive research design for 230 SACCOs. It was concluded that the board of directors and non-executive directors affected the financial performance in SACCOs while the board size and composition did not affect.

David, Scott, A., and Irem (2007) carried out a study to determine the association between typical measures of corporate governance and various accounting and economic outcomes in Asia. An exploratory research design was used for a sample of 2,106 firms and 39 structural measures of corporate governance consisting of board characteristics, stock ownership, institutional ownership, activist stock ownership, existence of debt holders, mix of executive compensation, and anti-takeover variables. The findings were that the variables had a mixed association with abnormal accruals, little relation to accounting restatements, but some ability to explain future operating performance and future excess stock returns.

Wan and Ong (2005) carried out a study to determine the relationship of board structure and firm performance. An exploratory research design was used for a sample of 212 publicly listed companies in Singapore. The findings were that no significant difference in performance of companies with or without role duality. Bonn, Yokishawa and Phan (2004) carried out a study on the relationship between board structure and firm performance. A descriptive research design was designed for 100 Japanese and Australian firms companies with key emphasis on the market to book ratio and return on assets. The findings established that a negative relationship exists between board size and firm performance and a positive relationship on the ratios of outside directors and female directors to the total board numbers.

2.7 Conceptual Framework

Corporate governance is of essence in all organisations despite the industry, size or level of growth. Their establishment forms a basis that affects the core operation and existence of an institution. In view of this, the study seeks to establish the relationship between the selected corporate governance principles and financial performance in investment banks. The conceptual framework thus shows the relationship between the independent and dependent variables as shown below.

INDEPENDENT VARIABLES **DEPENDENT VARIABLES**

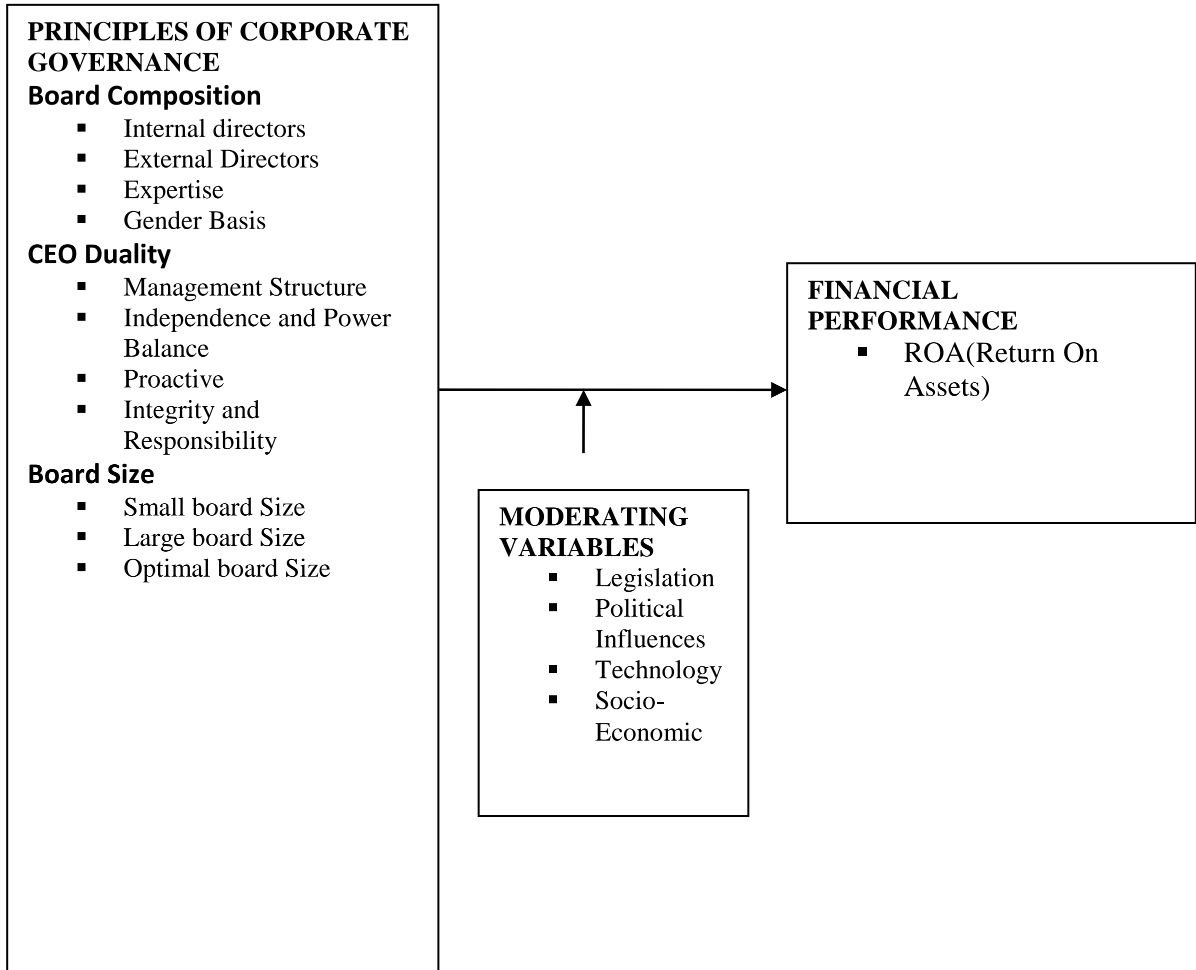

Figure 2.1 Conceptual Framework

(Source; Author, 2015)

The selected corporate governance principles constitute the independent variables. Firstly, the board composition focuses on the expertise of directors with the corresponding gender combination and the respective external versus internal members of the board. Secondly, the CEO duality in the institutions entails the management structure, independence, power balance, proactive and responsibility among the management. Lastly, board size encompasses the small or large board member number and the optimal board in line with the institutions' goals.

The influence of the independent on the dependent variables is based on the agency theory since it is based on a contract between the shareholders as the principal and board of directors or managers as the agents with the underlying objective of maximising returns on assets. This is attained by the shareholders incurring agency costs through the institutionalisation of corporate governance principles in line with moderating variables such as legislation, political influences, technology and socio-economic factors.

The dependent variable on the other hand is the financial performance. The measurement of the financial performance is the return on assets. The variable therefore is affected by the independent variables with the moderating variables in that the implementation is likely to influence positive financial performance while the non-implementation is likely to influence negative financial performance of the institutions. The study hence seeks to establish the relationship that exists between the variables.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

This chapter covers the research design, target population, data collection, data analysis and data presentation.

3.2 Research Design

The study used a descriptive research design which was appropriate for the study since it involved collecting data in order to test the hypothesis or answer questions concerning the current status of the variables with no manipulation (Mugenda & Mugenda, 2003).

Kavyula, Miring'u, A. and Muoria, E., (2011) studies were successfully analysed using the descriptive research design and proven appropriate. The study hence adopted the research design based on these prior studies. The study therefore generalised the findings to the larger population with the main focus on quantitative aspects while qualitative aspects was used to enhance understanding.

3.3Target Population

According to Mugenda and Mugenda (2003), target population is the members of a real or hypothetical set of people, events or objects the researcher wishes to generalize the results of the research.The target population consisted of seven investment banks licenced by the NSE and CMA since they had a high growth nature in the investment market and possess the

specialised capacity evidenced by managerial capability to develop innovative financing solutions to steer investment activities to great heights with a sufficient capital base.

The study focused on six management staff in each of the investment banks located within Nairobi County. This was necessitated by their accessibility of the required information and their direct involvement in the running of the investment banks for the study.

3.4 Data Collection

The study used both primary data and secondary data. For the primary data a structured questionnaire was administered to the top, middle and low level managers in investment banks within Nairobi County with a view to collect desired data. The top, middle and bottom level managers formed the three main strata identified with specific codes for the study while the respondents in each were randomly picked within investment banks in the NSE within Nairobi County constituting forty two respondents since they possessed the required characteristics.

The respondents' size is as presented in table 3.1 below

Table 3.1 Respondents Size

STRATA OF MANAGEMENT		TOTAL RESPONDENTS
TOP	1*7	7
MIDDLE	2*7	14
BOTTOM	3*7	21
TOTAL		42

Source: Author (2015)

According to Mugenda and Mugenda, (2003) questionnaires give relatively objective answers to complex problems. They are also a popular method for data collection due to the relative ease and cost effectiveness with which they are constructed and administered. In this study therefore a questionnaire was the main instrument of data collection from the staff members. It consisted of two main sections mainly the demographics that gave the general features of the company and the respondents while the other section outlined the objectives.

The objectives entailed a minimum of five questions with a maximum of ten questions in the form of a 5-likert scale (strongly agree to strongly disagree) and one open ended question.

The secondary data was based on the published financial statements such as statement of financial position, statement of financial performance and the cash flow for the period 2010 to 2013. The data of concern was the net income and average assets for the respective periods. In addition, the statements on corporate governance outlined in the company's financial statement reports were a key source of information.

3.5 Instrument Reliability and Validity

The researcher carried out a pilot study to pre-test the validity and reliability of data collected using the questionnaire. According to Berg and Gall (1989) validity is the degree by which the sample of test items represents the content the test is designed to measure. Content validity which was employed by this study is a measure of the degree to which data collected using the questionnaire represented the relationship between the stated corporate governance principles and shareholder returns. This was accomplished with the help of experts and examiners in the Faculty of Commerce at Egerton University.

According to Shanghverzy (2003) reliability refers to the consistency of measurement and is frequently assessed using the test–retest reliability method. Reliability was therefore increased by the similarity of responses in the questionnaire among the staff in the investment banks listed. The reliability was measured using Cronbach's alpha by the help of the statistical package for social sciences (SPSS). Struwig and Stead (2001) describe Cronbach's alpha as a measurement of how well a set of items measure a single one-dimensional talent construct and dichotomous type. According to Struwig and Stead (2001), for consistency to be present, the alpha must be 0.7 or above.

3.6 Data Analysis

Before processing the responses, data was edited, then coded and entered into a spreadsheet and analyzed using quantitative techniques. The quantitative data collected was analysed by the use of mean, mode, median, standard deviation, percentages and spearman correlation coefficient as per the section in the questionnaire. The demographic section was analysed using the mean, mode and percentages. The objectives captured in the likert scale were discussed using the mean, standard deviation and correlation coefficient while the relationship was established through simple regression analysis.

The model will be as below:

ROAib= a + b1BC + b2CD + b3BS + e

Where:

ROAib = Return on Assets

BC = Board Composition

CD = CEO Duality

BS = Board Size

3.7 Data Presentation

Analysed data was presented using tables, graphs and charts. The demographic data was presented in form of tables and charts while the objectives in form of tables and graphs to clearly outline the relationship between variables. These methods were seen as appropriate to represent the acquired information from the field so that it can be well understood.

CHAPTER FOUR

DATA ANALYSIS, PRESENTATION AND INTERPRETATION

4.1 Introduction

The chapter focuses on data analysis, presentation and interpretation. The data was gathered through questionnaires administered to forty two (42) respondents drawn from the seven licensed investment banks in Nairobi County. Results are presented in pie charts, tables and graphs. The findings of the study were organized based on specific objectives.

4.2 Response Rate

Table 4.1: Response Rate

Response	**Frequency**	**Percentage (%)**
Responded (Valid)	36	85.7
Responded (Invalid)	4	9.5
No Response	2	4.8
Total	**42**	**100**

Source: Field Data (2015)

As per the table 4.1 above, the target respondents for the study were the management staff of the licensed investment banks. The researcher thus administered forty two (42) questionnaires out of which thirty six (36) were considered valid for analysis, giving an 85.7% (36 respondents), invalid 9.5% (respondents) and no response 4.8% (2 respondents). This is in agreement with what was indicated by Cooper and Schindler (2003) who indicated that a response rate between 30 % and 80% of the total sample size can be generalised to represent the opinion of the entire population.

4.3 Demographic Data

In this section the study sought to determine the respondents' demographics information that was enquired for in the questionnaire such as position in management, gender, period of operation, core activities and bases of corporate governance.

4.3.1 Position in Management

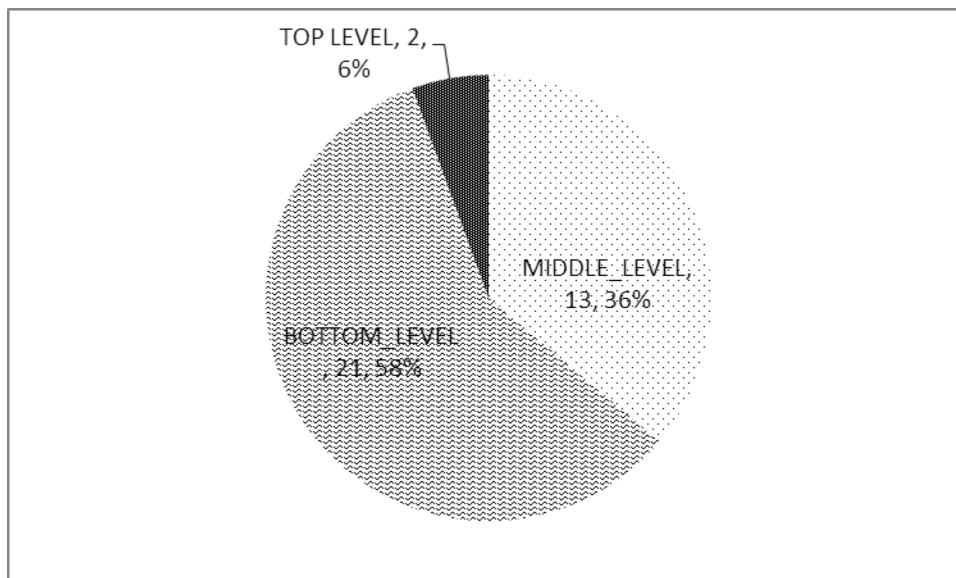

Figure 4.1: Position in Management

From figure above, the researcher found out that most of the respondents were in the bottom management constituting 58.3% (21 respondents), 36.1 % of the respondents (13 respondents) in the middle level while 5.6% (2 respondents) in top management. This is an indication that the bottom and middle level management are mainly involved in running of the activities in the investment banks hence were key to getting important data for the study.

4.3.2 Gender

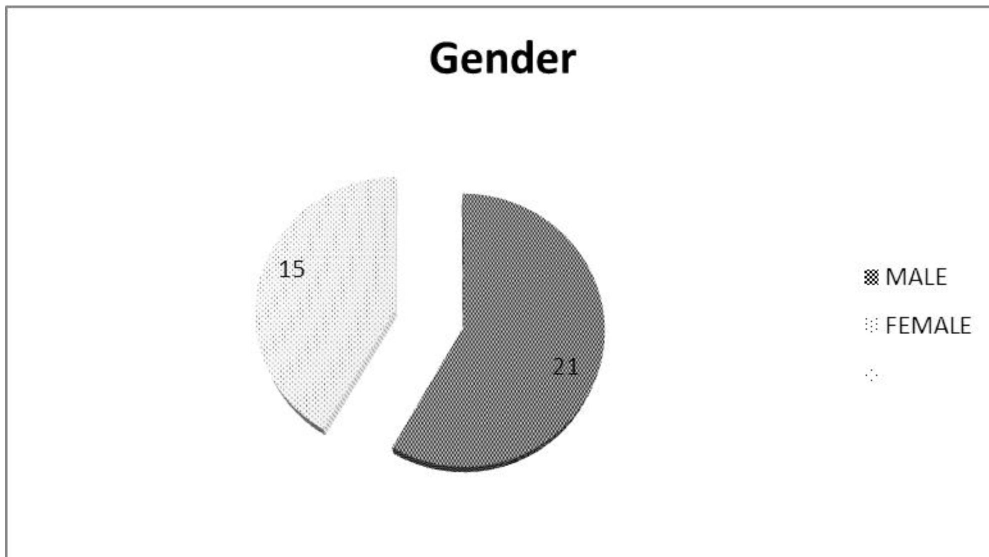

Figure 4.2: Gender

From the pie chart above, the respondents in regards to gender constituted of the highest mode as male (21 respondents) with the least mode being female (15 respondents). This indicated that the management composition in the investment banks comprised of more male than women.

4.3.3 Duration Of Operation

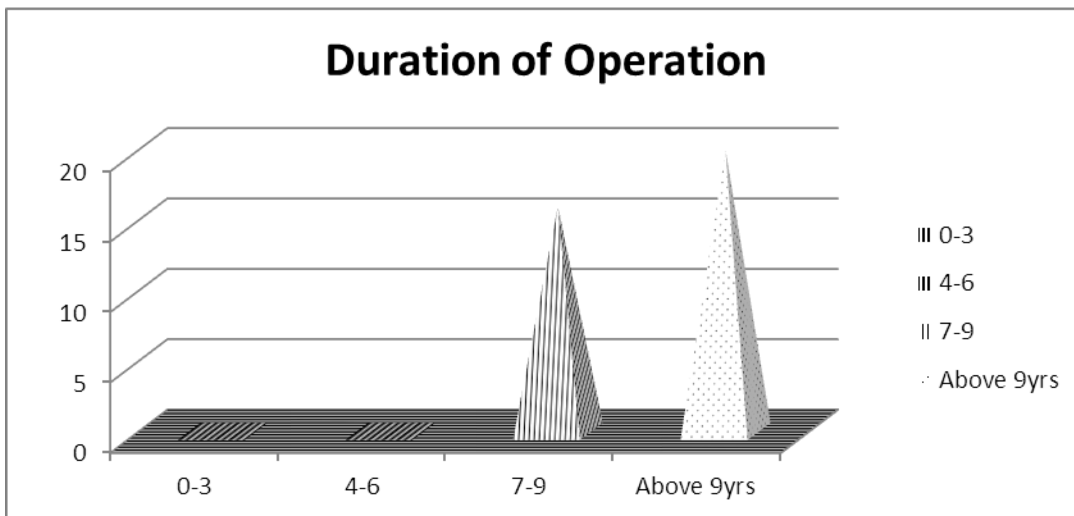

Figure 4.3: Duration of Operation

From the graph above, the researcher sought to determine the period in which the investment banks for the study have been in operation. Most of the investment banks, 44.4% (16 respondents) have been operating for a period of 7 to 9 years whereas 55.6% (20 respondents)

had operated for over 9 years. This is an indication of the considerable experience based on the long duration by the investment banks thus suitable in relevant data for the study.

4.3.4 Core Activities

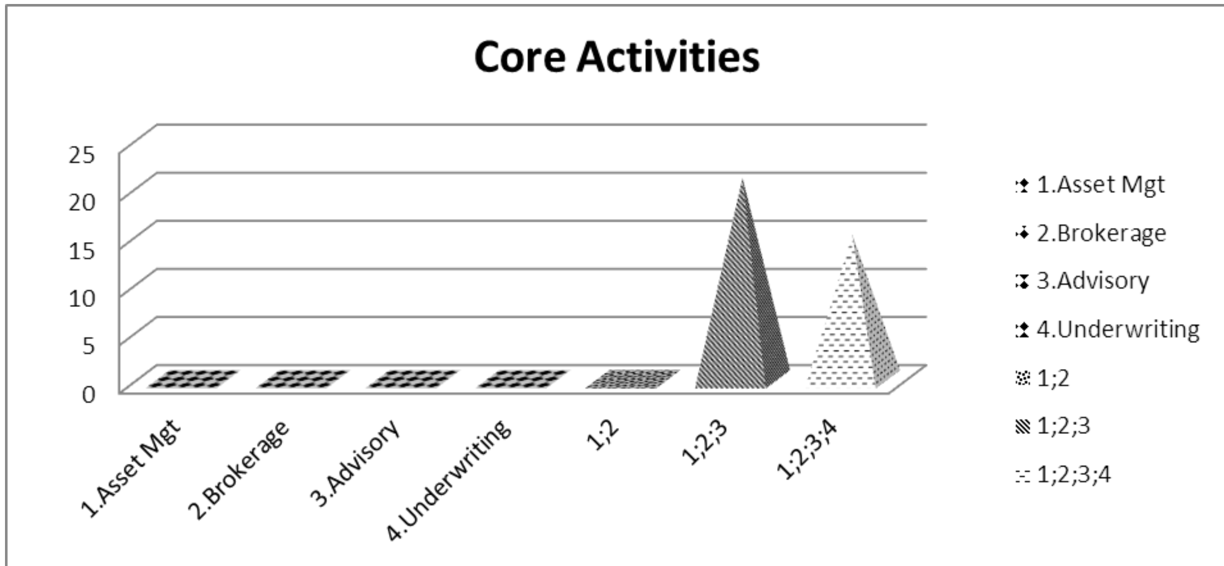

Figure 4.4: Core Activities

From the graph above, the researcher found out that majority, 58.3% (21 respondents) dealt in asset management, brokerage and corporate advisory whereas 41.7 % (15 respondents) provided asset management, brokerage, corporate advisory and underwriting services. This therefore implies that the investment banks in the study provided more than one service for their clients.

4.3.5 Bases of Corporate Governance

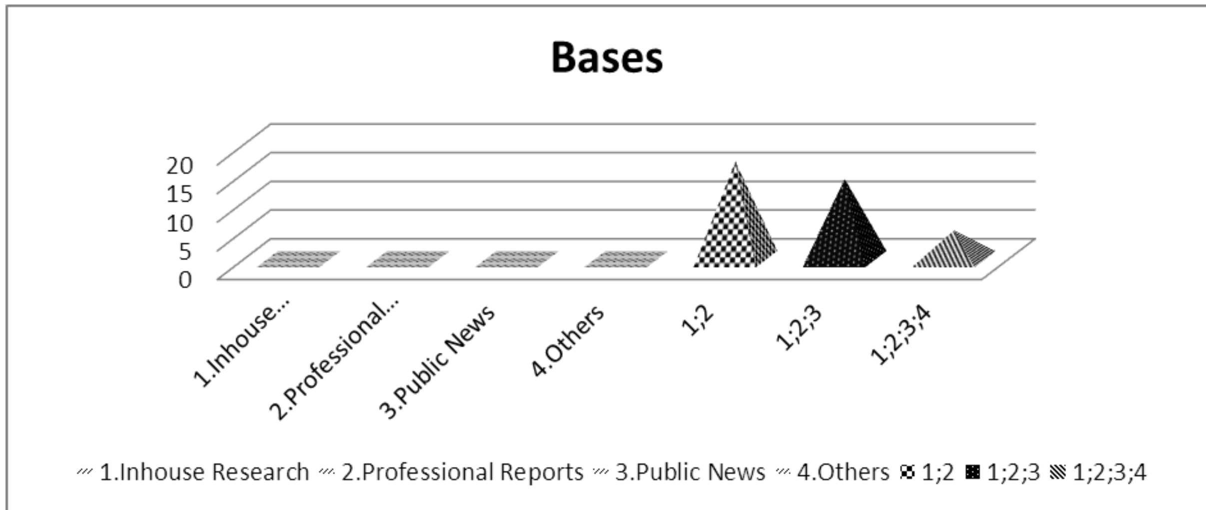

Figure 4.5: Bases of Corporate Governance

From the graph above, the respondents indicated on what basis the company's corporate governance was determined. On average, 47.2% (17 respondents) indicated in-house research and professional reports, 38.9 % (14 respondents) stated in-house research, professional reports and public news while 13.9 % (5 respondents) stated in-house research, professional reports, public news and other sources. This indicated that in-house research and professional reports for the investment banks was a key source for corporate governance variables for the study.

4.4 Research Objectives and Financial Performance

In this section, the study sought to determine whether any relationship exists between the selected corporate governance principles that were the independent variables and financial performance which was the dependent variable.

4.4.1 Board Composition

To evaluate the relationship between board composition and financial performance respondents were presented with six statements on a five point likert scale and asked to state their agreement with each statement. The responses of the corporate governance principle were accessed on a scale from 1 (Strongly Agree) through to 5 (Strongly Disagree). The percentages, means and standard deviation for each variable were calculated and results were presented in table below.

Table 4.2: Rating on Board Composition

	1	2	3	4	5	Mean	Standard Deviation
The company provides sufficient and timely information on the qualifications for board membership	8.3%	86.1%	5.6%	0	0	1.97	.377
The company has competent board of directors with requisite skills and expertise that enhance shareholder confidence in investments decisions	86.1%	13.9%	0	0	0	1.14	.351
The company's board member composition has outside directors that are key in contributing to the company performance.	38.8%	55.6%	5.6%	0	0	1.67	.586
The board members constitute a quorum involved in decisions of key investment projects in line with investor needs	5.6%	66.6%	27.8%	0	0	2.22	.540
The board gender basis affects the financial performance of the investment bank	25%	44.5%	8.3%	22.2%	0	2.28	1.085
The board has non-executive members who influence shareholder returns for the investments held in a financial period	0	58.3%	36.2%	5.5%	0	2.47	.609
Overall Mean						1.9583	
Overall Standard Deviation							0.591

From the above table, 86.1% of the respondents agreed on the company providing sufficient and timely information on the qualifications of board membership with 8.3% strongly

agreeing giving a total of 94.4 % for those who agreed while 5.6% neither agreed nor disagreed. 86.1 % of the respondents strongly agreed on having competent board of directors with requisite skills and expertise that enhance shareholder confidence in investment decisions while 13.9% agreed with the statement. Those rated to agree with the board member composition consisting of outside directors, who are key in contributing to the company performance were 55.6% with 38.8% agreeing while 5.6% neither agreed nor disagreed. 66.6% agreed with the constitution of a quorum in making decisions of key investment projects in line with investor needs while 5.6% strongly agreed with the statement giving a total of 72.2% for those who agreed while 27.8% neither agreed nor disagreed. 44.5% of the respondents agreed on the gender basis affecting the firm financial performance with 25% strongly agreeing, 22.2% disagreed while 8.3% neither agreed nor disagreed. 58.3% agreed on the board constituting non-executive members who influence shareholder returns, 36.2% neither agreed nor disagreed while 5.5% disagreed with the statement.

From the standard deviations obtained, the board constituting competent board members with requisite skills had the lowest with 0.351 followed by the provision of sufficient and timely information on board membership with 0.377. Therefore board members competence and the timely provision of requisite information were the main factors for board composition influencing financial performance. The gender basis affecting financial performance had the highest standard deviation of 1.085 hence lowest factor of board composition influencing financial performance.

4.4.2 CEO Duality

To evaluate the relationship between CEO duality and financial performance respondents were presented with six statements on a five point likert scale and asked to state their agreement with each statement. The responses of the corporate governance principle were accessed on a scale from 1 (Strongly Agree) through to 5 (Strongly Disagree). The percentages, means and standard deviation for each variable were calculated and results were presented in table below.

Table 4.3: Rating on CEO Duality

	1	**2**	**3**	**4**	**5**	**Mean**	**Standard Deviation**
The CEO position	13.9%	77.8%	8.3%	0	0	1.94	.475

influences the firm performance through the assurance of creating value for shareholder investments							
The CEO and Chairman roles are clearly outlined and understood on a firm-wide basis through an effective corporate system	11%	52.8%	16.7%	16.7%	2.8%	2.47	1.00
The board ensures that the CEO and Chairman positions are held by different persons hence distribution of power that assures independent judgment	0	77.8%	16.7%	5.5%	0	2.28	.566
The board actively provides clear guidelines of the CEOs influence of shareholder returns for the investments held in a financial period	0	50%	44.4%	5.6%	0	2.56	.607
The board ensures that a proper a management structure is in place and make the structure function to maintain corporate integrity, reputation and responsibility	38.9%	61.1%	0	0	0	1.61	.494
The board ensures that the CEO remuneration is aligned to their performance hence the	11.1%	52.8%	36.1%	0	0	2.25	.649

efficiency in management of the firm financial resources							
Overall Mean						2.185	
Overall Standard Deviation							0.6318

From the table above, 77.8% of the respondents agreed the CEO position influences firm performance through the assurance of creating value for shareholder investments with 13.9% strongly agreeing with this statement giving a total of 91.7% for those who agreed while 8.3% neither agreed nor disagreed. 52.8% of the respondents agreed that the CEO roles are clearly outlined and understood on a firm-wide basis through an effective corporate system with 11% strongly agreeing while 16.7% neither agreed nor disagreed as well as disagreeing and 2.8% strongly disagreed.77.8% of the respondents agreed that the board ensures that the CEO and Chairman positions are held by different persons assuring independence while 16.7% neither agreed nor disagreed and 5.5% disagreed with the statement.50% of the respondents agreed that board actively provides clear guidelines of the CEOs influence of shareholder returns for the investments while 44.4% neither agreed nor disagreed and 5.6% disagreed with the statement.

61.1% of the respondents agreed with the board ensuring a proper a management structure is in place that maintains corporate integrity, reputation and responsibility while 38.9% strongly agreed with the statement. 52.8% of the respondents agreed the board ensures that the CEO remuneration is aligned to their performance hence the efficiency of financial resources with 11.1% strongly agreeing while 36.1% neither agreed nor disagreed with the statement.

From the standard deviations obtained, the CEO position influencing firm performance through the assurance of creating value for shareholder investments had the lowest with 0.475 followed by the board ensuring a proper a management structure is in place that maintains corporate integrity, reputation and responsibility with 0.494. Therefore the CEO position and the management structure were the main factors for CEO duality influencing financial performance. The outlining of the CEO and Chairman roles on a firm wide basis had the highest standard deviation of 1.00 hence lowest factor of CEO duality influencing financial performance.

4.4.3 Board Size

To evaluate the relationship between board size and financial performance respondents were presented with five statements on a five point likert scale and asked to state their agreement with each statement. The responses of the corporate governance principle were accessed on a scale from 1 (Strongly Agree) through to 5 (Strongly Disagree). The percentages, means and standard deviation for each variable were calculated and results were presented in table below.

Table 4.4: Rating on Board Size

	1	**2**	**3**	**4**	**5**	**Mean**	**Standard Deviation**
The company has a clear guideline for the provision of the appropriate number of board members that enhances the company's goals.	2.8%	66.7%	30.5%	0	0	2.28	.513
The board members in the company consist of five or less members which is valued as a small board size.	55.6%	44.4%	0	0	0	1.44	.504
The board members in the company are more than five which is valued as a large	0	0	0	47.2%	52.8%	4.53	.506

board size.							
The number of board members is sufficient to support the company's operations and procedures.	38.9%	50%	11.1%	0	0	1.72	.659
The determined number of board members in the company is optimal in influencing financial performance.	44.4%	50%	5.6%	0	0	1.61	.599
Overall Mean						2.316	
Overall Standard Deviation							0.5562

From the table above, 66.7% of the respondents agreed that the company has a clear guideline for the provision of the appropriate number of board members with 2.8% strongly agreeing thus a total of 69.5% of those who agreed while 30.5% neither agreed nor disagreed. 55.6% strongly agreed that board members in the company consist of five or less members valued as a small board size with 44.4% agreeing with the statement. 52.8% of the respondents strongly disagreed that the board members in the company are more than five valued as a large board size while 47.2% disagreed with the statement.50% of the respondents agreed with the number of board members as sufficient to support the company's operations and procedures with 38.9% strongly agreeing giving a total of 88.9% agreeing while 11.1% neither agreed nor disagreed. 50% of the respondents agreed that the determined number of board members in the company is optimal in influencing financial performance with 44.4% strongly agreeing giving a total of 94.4% of those who agreed while 5.6% neither agreed nor disagreed with the statement.

From the standard deviations obtained, board members in the company consisting of five or less members valued as a small board size had the lowest with 0.504 followed by the board members in the company are more than five valued as a large board size with 0.506. Therefore the board member number was the main factors for board size in influencing financial performance. The optimal nature of the board members in supporting the company

operations had the highest standard deviation of 0.659 hence lowest factor of board size influencing financial performance.

4.5 Reliability Test

The reliability of the variables of corporate governance was measured using the Cronbanch's alpha by the help of the statistical package for social sciences (SPSS).

Table 4.5: Cronbanch's Alpha for the Variables

	No. of Items	Cronbach	Mean	Standard Deviation
Board Composition, CEO Duality and Board Size	17	0.778	2.144	0.388

From table 4.5, the Cronbach alpha value was 0.778 which indicated high reliability on the relationship of the variables. According to Struwig and Stead (2001), for consistency to be present, the alpha must be 0.7 or above. The number of items consists of the questions in the questionnaire for the three objectives totalling to seventeen with a high mean of 2.144 with a low standard deviation of 0.388.

4.6 Return On Assets

Secondary data was collected from the Nairobi Securities Exchange (NSE) for the firm's financial statements for the years between 2010 and 2013. The study collected data on Return On Assets as a dependent variable which was measured as the amount of net income returned as a percentage of average total assets.

Table 4.6: Return On Assets

YEAR Company	2010	2011	2012	2013	ROA (Mean)	Standard Deviation
African Alliance	-0.05	-0.16	0.15	0.13	0.02	0.15

Kenya Investment Bank Ltd						
Dyer & Blair Investment Bank Ltd	0.09	0.01	0.05	0.01	0.04	0.04
Faida Investment Bank Ltd	0.04	-0.004	0.004	0.01	0.01	0.02
Renaissance Capital Ltd	-0.12	0.14	0.06	0.01	0.02	0.11
Sterling Capital Ltd	0.08	0.02	0.09	0.03	0.05	0.04
Standard Investment Bank Ltd	0.03	0.01	0.02	0.02	0.02	0.01
Suntra Investment Bank Ltd	0.04	-0.03	-0.02	0.02	0.003	0.03

Source: Nairobi Securities Exchange (2010-2013)

Table 4.6 above shows the return of assets for each of the seven investment banks in the NSE for the period 2010 to 2013. In African Alliance Kenya investment bank ltd, the ROA grew from the negative to the positive with its lowest in 2011 at (0.16) with the highest at 0.15 in 2012; the mean for the period was 0.02 and the standard deviation at 0.15. In Dyer and Blair investment bank ltd, the ROA was maintained on the positive with the lowest in 2011 and 2013 at 0.01 with the highest at 0.09 in 2010; the mean and standard deviation for the period were at 0.04. In Faida investment bank ltd, the ROA was averagely positive with the lowest in 2011 at (0.004) with the highest in 2010 at 0.04; the mean was at 0.01 and standard deviation for the period at 0.02.

In Renaissance Capital ltd, the ROA was averagely positive with the lowest at (0.12) in 2010 with the highest at 0.14 in 2011; the mean was at 0.02 and standard deviation for the period at 0.11. In Sterling Capital ltd, the ROA was stable on the positive with the lowest in 2011 at 0.02 with the highest at 0.09 in 2012; the mean was at 0.05 and standard deviation for the period was at 0.04. In Standard investment bank ltd, the ROA was maintained on the positive with the lowest in 2011 at 0.01 with the highest at 0.03 in 2010; the mean was at 0.02 and standard deviation for the period was at 0.01. In Suntra investment bank ltd, the ROA was relatively positive with the lowest in 2011 at (0.03) with the highest at 0.04 in 2010; the mean was at 0.003 and standard deviation for the period was at 0.03.

For the period 2010 to 2013 the lowest ROA for majority of the investment banks was in 2011with the lowest as (0.004) in Faida investment bank ltd while the highest ROA for most of the firms was in 2012 with the highest as 0.15 in African Alliance Kenya investment bank ltd. For the mean for the period 2010 to 2013 the companies maintained a positive return with the highest in Sterling Capital ltd at 0.05 with the lowest in Suntra investment bank ltd at 0.003. On the standard deviation for the period, the lowest was in Standard investment bank ltd at 0.01 with the highest in African Alliance Kenya investment bank ltd at 0.15.

Table 4.7: Overall Descriptive Statistics

Statistics / Variables	Mean	Standard Deviation
Board Composition	1.958	0.591
CEO Duality	2.185	0.632
Board Size	2.316	0.556
ROA	0.02	0.056

In table 4.7 above, the overall means for the independent variables and dependent variables were assessed. For the means, the independent variables had the highest compared to the dependent variable with the highest as 2.316 on board size, 2.185 on CEO duality, 1.958 on board composition with the lowest for ROA as 0.02. This implies the high reliability of the independent variables for the study. On the other hand, the overall standard deviation for the dependent variable with the lowest as 0.056 while the independent variables as 0.556 on board size, 0.591 on board composition and 0.632 on CEO duality. This is indicated the high consistency of the results for the dependent variable for the study.

4.7 Correlation Analysis

Table 4.8: Correlation Matrix

		ROA	BC	CEO	BS
ROA	Pearson Correlation	1	-.426**	-.825**	-.201
	Sig. (2-tailed)		.010	.000	.239
	N	36	36	36	36
BC	Pearson Correlation	-.426**	1	.749**	.142
	Sig. (2-tailed)	.010		.000	.407
	N	36	36	36	36
CEO	Pearson Correlation	-.825**	.749**	1	.417*
	Sig. (2-tailed)	.000	.000		.011
	N	36	36	36	36
BS	Pearson Correlation	-.201	.142	.417*	1
	Sig. (2-tailed)	.239	.407	.011	
	N	36	36	36	36

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

* Correlation is significant at the 0.05 level (2-tailed)

On the correlation of the study variables the researcher conducted a Pearson correlation as shown in table 4.8. From the findings on the correlation analysis between ROA and the various corporate governance principles the study found out that there was negative correlation coefficient between ROA and Board composition shown by correlation coefficient of ($r= -0.426, p< 0.01$) which is statistically significant at 99% confidence level. There is a

strong negative correlation between ROA and CEO duality as shown by a correlation of(r= -0.825, p< 0.01) which is statistically significant at 99% confidence level .There is a weak negative correlation between ROA and Board size with a correlation coefficient of(r= -0.201, p> 0.01) which is not statistically significant at 99% confidence level. This is an indication that there was a negative relationship between Board composition, CEO duality and Board size with financial performance of investment banks.

4.8 Regression Analysis

Regression analysis was used to determine the predictive power of board composition, CEO duality and board size on financial performance in investment banks. The three independent variables were regressed against the dependent variable on a simple linear regression analysis. Model summary table below shows the coefficient of determination (R^2) which explains the percentage of variation in investment banks financial performance.

Table 4.9: Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.909[a]	.825	.809	.00613

a. Predictors: (Constant), BS, BC, CEO

From the table above, the regression model containing board size, board composition and CEO duality as the predictor variables explains 82.5% of the variation in investment banks financial performance. The remainder (17.5%) can be explained by other factors not included in the model.

The table below displays the ANOVA results that test the significance of the R^2 for the model.

Table 4.10: ANOVA

Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	.006	3	.002	50.456	.000[b]

	Residual	.001	32	.000		
	Total	.007	35			

a. Dependent Variable: ROA

b. Predictors: (Constant), BS, BC, CEO

An F statistics of 50.456 with a p value less than 5 % significance level indicates that the overall model was statistically significant at 95% confidence level.

The table of coefficients below presents the unstandardized and standardized coefficients of the model, t statistic for each coefficient and the associated p values. The predictor variables had significant positive relationship for board composition and size with significant negative relationship for CEO duality with financial performance of investment banks.

Table 4.11: Coefficients

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	.135	.027		5.005	.000
	BC	.049	.010	.546	4.705	.000
	CEO	-.140	.013	-1.353	-10.695	.000
	BS	.042	.012	.285	3.365	.002

The model that was used by the study was;

ROAib= a + b1BC + b2CD + b3BS + e

Where:

ROAib = Return on Assets

BC = Board Composition

CD = CEO Duality

BS = Board Size

From the data in the table the established regression equation was;

ROAib = 0.135 + 0.049 BC – 0.140 CD + 0.042 BS

From the above regression equation, it was revealed that board composition, CEO duality and board size to a constant zero, financial performance of investment banks would stand at 0.135. A unit increase in board composition would lead to a 0.049 increase in financial performance (ROA) of investment banks, a unit increase in CEO duality would lead to a

0.140 decrease in financial performance (ROA) of investment banks and a unit increase in board size would lead to a 0.042 increase in financial performance (ROA) of investment banks. These findings support those of Miring'u, A. and Muoria, E. (2011) who identified that a positive relationship exists between return on equity (ROE) and board size and board compositions of all state corporations and Maulu (2014) whose findings were that a relationship exists between different aspects of corporate governance practices and financial performance.

4.9 Testing Hypothesis

The first hypothesis was, $Ho_{1;}$ there is no relationship between board composition and financial performance of investment banks in the NSE. This hypothesis was tested at 5% significance level which was rejected since the p value = 0.000 was less than 5% with t= 4.705. Therefore there is a significant positive relationship between board composition and financial performance.

The second hypothesis was $Ho_{2;}$ there is no relationship between CEO duality and financial performance of investment banks in the NSE. This hypothesis was tested at 5% significance level which was rejected since the p value = 0.000 was less than 5% with t= -10.695. Therefore there is a significant negative relationship between CEO duality and financial performance.

The third hypothesis was Ho_3; there is no relationship between board size and financial performance of investment banks in the NSE. This hypothesis was tested at 5% significance level which was rejected since the p value = 0.002 was less than 5% with t= 3.365. Therefore there is a significant positive relationship between board size and financial performance.

In conclusion, the hypothesis that corporate governance principles have no relationship on financial performance in investment banks was rejected since the predictor variables of the model, board composition, CEO duality and board size with their combined contribution, were significant at 5% significant level.

CHAPTER FIVE

SUMMARY OF FINDINGS, CONCLUSION AND RECOMMENDATIONS

5.1 Introduction

The chapter presents the summary and discussions of the findings of the study and it also gives the conclusions and recommendations of the study based on the objectives of the study. The purpose of this study was to assess the relationship between selected corporate governance principles and financial performance of investment banks in the NSE. Specifically, the study sought to establish the relationship between board composition and financial performance of investment banks in the NSE, to determine the relationship between CEO duality and financial performance of investment banks in the NSE and to determine the relationship between board size and financial performance of investment banks in the NSE.. A conclusion based on the findings was made with recommendations from the above objectives.

5.2 Summary of findings

Based on the objectives of the study stated in the introduction above, the following are the summary of findings of the results obtained from the data analysed.

5.2.1: To establish the relationship between board composition and financial performance

According to the research results, board composition influences financial performance in investment banks in the NSE. The competency of the board and sufficiency of information on qualification for board membership was found necessary for investment banks. The results showed that at 5% level of significance, board composition played a significant role in determining financial performance in investment bank in the NSE, where a unit increase in board composition led to a 0.049 increase in financial performance thus the regression analysis findings indicated a positive relationship between board composition and financial performance. The study rejected the null hypothesis that there is no relationship between board composition and financial performance of investment banks in the NSE. These findings

support those of Dehaena et al. (2001), Omar (2003) and Rhoades et al. (2000) who found that board composition (proportion of independent directors on the board) has a positive relationship with financial performance.

5.2.2: To determine the relationship between CEO Duality and financial performance

According to the research results, the study found that CEO duality influences financial performance in investment banks in the NSE. It was observed that the CEO position, the management structure and separation of the CEO and chairman position influenced performance of investment banks in the NSE. The results showed that at 5% level of significance, CEO duality played a significant role in determining financial performance in investment bank in the NSE, where a unit increase in CEO duality led to a 0.140 decrease in financial performance. The regression analysis findings thus indicated a negative relationship between CEO duality and financial performance. The study rejected the null hypothesis that there is no relationship between CEO duality and financial performance of investment banks in the NSE. These findings support those of Bernstein (2004) who concluded that the split of roles of Chairman and CEO performed better than those companies which have the same individual in both positions. Amba (2013) opined CEO duality has a negative impact on business performance with regard to ROA, ROE, and Assets turnover.

5.2.3: To determine the relationship between board size and financial performance

The research results for the objective indicate that the board size influences financial performance in investment banks in the NSE. The results showed that at 5% level of significance, board size played a significant role in determining financial performance in investment bank in the NSE, where a unit increase in board size led to a 0.042 increase in financial performance. The correlation analysis findings indicated a positive relationship between board size and financial performance. The study rejected the null hypothesis that there is no relationship between CEO board size and financial performance of investment banks in the NSE. These findings concur with the findings of Vafeas (2000) that firms with the smallest boards (minimum of five board members) are better informed about the earnings of the firm thus better monitoring abilities.

5.3 Conclusion

The corporate governance principle that had the most significant relationship on financial performance was CEO duality mainly based on variables such as influence of CEO position on shareholder investment and the management structure. The second corporate governance principle which had a moderate significant relationship on financial performance was board composition mainly based on variables such as timely information on board member qualification and the competency of directors. The third corporate governance principle which had a moderate significant relationship on financial performance was board size based mainly on variables such as the number of board members as five or less and adherence on clear guidelines for the provision of appropriate number of board members. There was an overall positive contribution of the board composition, CEO duality and board size on the ROA.

5.4 Recommendations

Based on the research findings and conclusions drawn from this study, recommendations have been provided. The investment banks operations are required to be governed through a clear management structure. This is so as to enhance security of shareholder wealth and sustainability of the organisation. This could be achieved by continually reviewing regulations regarding management governance structures so as to assure transparency in limiting CEO duality thus assuring legitimacy in the firm performance.

The board members in investment banks should entail a pool of diverse skills and expertise to enhance innovative ways in steering business performance. This could be enhanced through independent recruitments from a pool of experts and the pre-allocation of equitable balance in the boards will assure diverse concepts and ideas in business performance. The board member number should be maintained on an optimal basis of five or less. The overall positive contribution of each independent variable to the dependent variable indicates the importance

of each. This thus requires institutions to invest in the optimal operationalization of the corporate governance focused in this study.

5.5 Areas for Further Research

Further research should focus on the limitations of this study since numerous expansions of this research are possible. First, the study focused only on three corporate governance features on their relationship on firm performance. The features covered are important while other diverse variables such as the financial reporting, management style and the audit committee could be examined with their impact on firm performance. The firm of study was limited to investment banks which form part of the financial sector thus further studies could be done on other institutions in the private and public sector.

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APPENDICES

Appendix I: Letter of Introduction

EGERTON UNIVERSITY,
FACULTY OF COMMERCE,
DEPARTMENT OF ACCOUNTING, FINANCE & MANAGEMENT SCIENCE,
P.O BOX 536- 20115
NAIROBI CAMPUS
DATE

TO: THE MANAGER
Dear Sir/Madam
RE: REQUEST FOR THE DATA COLLECTION

I am a student in Egerton University pursuing a Master's degree in Finance. As a requirement of the Master's degree, i seek to conduct a research of the relationship between selected corporate governance principles and financial performance of investment banks in the NSE.
It is my humble request to you to fill in the attached questionnaire. The information you give will be treated with utmost confidentiality and the results shall be for academic purposes only.
Your kind co-operation will be highly appreciated.
Yours faithfully,
Kellen Kamwaro

Appendix I I: Questionnaire

This questionnaire has been designed to help carry out research of the relationship between selected corporate governance principles and financial performance of investment banks in the NSE for purely academic purposes under the Masters in Business Administration programme. Your contribution to this research is highly valued and strictly confidential

PART A: Demographic Characteristics

1. What is the name of your company? (**Optional**)...

Please tick where applicable

2. What position in management do you hold?

   Top level [ ]   Middle level [ ]   Bottom level [ ]

3. What is your gender? Male [ ] Female [ ]

4. How long has the company operated as an investment bank?

   0-3 years [ ] 4-6 years [ ] 7-9 years [ ] Above 9 years [ ]

5. What are the core activities of the investment bank?

   Asset management [ ] Brokerage [ ] Corporate advisory [ ] Underwriting [ ]

6. What are the bases upon which you evaluate the corporate governance level of your company?

   In-house research [ ] Professional reports [ ] Public news [ ] Other [ ]

PART B: Corporate Governance Principles

Please rate by ticking each number below that denotes the extent of your agreement or disagreement with the following statements as represented on the scale of 1 to 5, where;

1. Strongly Agree 2. Agree 3. Neither agree nor disagree 4. Disagree
5. Strongly Disagree

Board Composition	**1**	**2**	**3**	**4**	**5**
1. The company provides sufficient and timely information on the qualifications for board membership.	☐	☐	☐	☐	☐
2. The company has competent board of directors with requisite skills and expertise that enhance shareholder confidence in investments decisions .	☐	☐	☐	☐	☐
3. The company's Annual Report includes a section devoted to the board member composition and their contribution to the company performance.	☐	☐	☐	☐	☐
4. The board members constitute a quorum are involved in decisions of key investment projects in line with investor needs.	☐	☐	☐	☐	☐
5. The board size and gender basis affects the financial performance of the investment bank.	☐	☐	☐	☐	☐
6. The board actively provides guidelines of distribution of shareholder returns for the investments held in a financial period.	☐	☐	☐	☐	☐

Please indicate any other point in relation to the stated corporate governance principle

....

....

CEO Duality	**1**	**2**	**3**	**4**	**5**
1. The CEO position influences the firm performance through the assurance of creating value for shareholder investments.	☐	☐	☐	☐	☐
2. The CEO and Chairman roles are clearly outlined and understood on a firm-wide basis through an effective corporate system.	☐	☐	☐	☐	☐
3. The board ensures that the CEO and Chairman positions are held by different persons hence distribution of power that assures independent judgement.	☐	☐	☐	☐	☐
4. The board actively provides clear guidelines of the CEOs influence of shareholder returns for the investments held in a financial period.	☐	☐	☐	☐	☐
5. The board ensures that a proper a management structure is in place and make the structure function to maintain corporate integrity, reputation and responsibility.	☐	☐	☐	☐	☐
6. The board ensures that the CEO remuneration is aligned to their performance hence the efficiency in	☐	☐	☐	☐	☐

management of the firm financial resources.

Please indicate any other point in relation to the stated corporate governance principles

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Board Size	**1**	**2**	**3**	**4**	**5**
1. The company has a clear guideline for the provision of the appropriate number of board members that enhances the company's goals.	☐	☐	☐	☐	☐
2. The board members in the company consist of five or less members which is valued as a small board size.	☐	☐	☐	☐	☐
3. The board members in the company are more than five which is valued as a large board size.	☐	☐	☐	☐	☐
4. The number of board members is sufficient to support the company's operations and procedures.	☐	☐	☐	☐	☐
5. The determined number of board members in the company is optimal in influencing financial performance.	☐	☐	☐	☐	☐

Please indicate any other point in relation to the stated corporate governance principles

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<u>THANK YOU FOR TAKING TIME TO RESPOND TO THIS QUESTIONNAIRE</u>

Appendix III : Work Plan

TIME FRAME	ACTIVITY
June – August 2014	Identification of research Topic Proposal Writing Submission and Discussion with the supervisor

September 2014- January 2015	Presentation of research proposal Data collection Data Analysis
February 2015- March 2015	Findings, conclusion and submitting the final research document

Appendix IV: Data Collection Sheet

RETURN ON ASSETS					
YEAR BANK	2010	2011	2012	2013	MEAN
African Alliance Kenya Investment Bank Ltd					
Dyer & Blair Investment Bank Ltd					
Faida Investment Bank Ltd					
Renaissance Capital Ltd					
Sterling Capital Ltd					
Standard Investment Bank Ltd					
Suntra Investment Bank Ltd					

Appendix V: Investment Banks Licensed by Capital Markets Authority In The Nairobi Securities Exchange

1. African Alliance Kenya Investment Bank Limited
2. Dyer & Blair Investment Bank Limited
3. Faida Investment Bank Limited
4. Renaissance Capital Limited
5. Sterling Capital Ltd
6. Standard Investment Bank Limited
7. Suntra Investment Bank Limited

Source: Nairobi Securities Exchange (NSE); Capital Markets Authority (CMA) (2014); Gazette Notice No.4938 Vol. CXV No. 4, 2011

Appendix VI: Budget

ITEM	COST (Ksh)
1. Internet Browsing, Printing and Binding	20,000
2. Transport Costs	5,000
3. Stationery	3,000
4. Miscellaneous Expenses	2,000
TOTAL	**30,000**